

## NEAR FINAL RULES: EXTENSION OF THE SENIOR MANAGERS AND CERTIFICATION REGIMES TO THE INSURANCE SECTOR

The FCA and PRA have published the near final rules on the extended senior managers and certification regimes ("**SMCR**") that will apply to all sectors of the insurance industry regulated by the FCA and/or PRA with effect from 10 December 2018 (subject to some transitional provisions in relation to certification and the conduct rules). The FCA has also published a "Guide for Insurers" that includes a SMCR "readiness checklist". Generally, the regulators have not made significant changes to the original proposals consulted on.

The full scope SMCR regime will apply to Solvency II firms and large Non Directive Firms ("**NDFs**") and a streamlined regime will apply to small NDF's, small run off vehicles and Insurance Special Purpose Vehicles ("**ISPVs**"). All insurers will be subject to the FCA Certification regime, Fit and Proper test obligations and Conduct Rules requirements.

Firms should start preparing for commencement of the new regime addressing what changes may need to be made to training, employment documents and compliance policies and procedures and what steps should be taken to ensure that senior individuals understand the obligations of the regime for them personally.

### Key features of the Insurance SMCR Regime

#### Full scope and streamlined regimes

- Regulatory pre-approval for senior managers
- Statements of responsibility for senior managers
- Personal accountability/duty of responsibility for senior managers
- Annual firm certification of individuals in 'Certified Function' roles from 10 December 2019
- A requirement to obtain regulatory references for senior managers, certified persons and non-executive directors (Solvency II firms and large NDF's are already subject to this obligation)
- New Conduct Rules will apply to a broad group of employees

#### Content

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- New notification, training and record-keeping obligations

#### Full scope regime only

- Handover procedures
- Additional prescribed senior manager responsibilities
- Management Responsibilities Map and a requirement to allocate "Overall Responsibility" to a senior manager for every activity, business area and management function of the firm

#### Is my firm affected?

Yes, if your firm is a Solvency II firm (including incoming branches of non-UK firms), a large or small NDF, an ISPV or a Society of Lloyds or Lloyds managing agent. All insurers regulated by the FCA and PRA are affected.

In scope firms will be subject to either the full scope SMCR or a streamlined version.

#### What are the key elements of the Insurance SMCR?

The SMCR will replace the current enhanced FCA Approved Persons Regime and Senior Insurance Managers Regime ("**SIMR**") for firms currently subject to these regimes.

Key aspects of the insurance SMCR are as follows:

#### Senior Managers

- The FCA has designated five executive and two non-executive roles as 'Senior Management Functions' ("**SMFs**") (Executive Director, Other Overall Responsibility, Conduct Risk Oversight Officer, Compliance Oversight and Money Laundering Reporting Officer (MLRO), Chair of the Nomination Committee and Chair of the with Profits Committee). The PRA will maintain the existing Senior Insurance Management Functions (SIMF's) which will be relabelled SMFs.
- Anyone holding a PRA or FCA, SMF will be subject to pre-approval by the relevant regulator (individuals currently holding these roles will not require approval on commencement of the new regime under 'grandfathering' arrangements). The FCA has recommended that firms should have the appropriate people in the correct approved function before the move to the new regime. (There is a modified regime for incoming EEA and non EEA branches).
- In addition to the prescribed responsibilities as part of SIMR, certain additional responsibilities prescribed by the FCA will need to be allocated amongst the senior managers ("**SMs**") on a legal entity basis, rather than on a group basis.
- Each SM's individual role and responsibilities will need to be set out in a 'statement of responsibilities' ("**SoR**") which must be submitted to the regulators with the SM's approval application (subject to grandfathering arrangements). Currently, key function holders ("**KFHs**") at Solvency II firms and large NDF's are required by the PRA to maintain a 'Scope of Responsibilities' document; this will be renamed a Statement of Responsibility and the obligation will be extended to ISPV's. Whenever

#### Publications

The FCA has published the following three policy statements:

- [PS18/14: Extending the Senior Managers & Certification Regime to FCA Firms – Feedback to CP17/25 and CP17/40, and near-final rules;](#)
- [PS18/15: Extending the Senior Managers & Certification to insurers – Feedback to CP17/26 and CP17/41 and near-final rules;](#) and
- [PS18/16: Insurers and FCA solo-regulated firms Final Guidance: the Duty of Responsibility for insurers and FCA solo-regulated firms.](#)
- It is also proposing to introduce a new directory of financial services workers (see [CP18/19: Introducing the Directory](#)). The directory will be a public register designed to help consumers and firms check the status and history of individuals working in financial services. The deadline for responses to the consultation is 5 October 2018.

The PRA has published PS15/18:

- [Strengthening individual accountability in insurance: Extension of the Senior Managers and Certification Regime to insurers.](#) PS15/18 provides feedback on proposals for extending the SMCR to insurers.

there is a 'significant change' in a firm's management arrangements every affected SM will have to update their SoR, with the PRA updating their guidance to clarify what would constitute a 'significant change'.

- Senior managers will have a statutory 'Duty of Responsibility' and will potentially be accountable if they fail to take reasonable steps to prevent a breach by a firm in their area of responsibility as set out in their statement of responsibilities.
- A criminal records check will have to be undertaken in respect of each senior manager approval application. (FCA requirement only)
- Full scope SMCR firms will be required to ensure there is a senior manager with overall responsibility for every area, business activity and management function (the 'Overall Responsibility' requirement). This should be the most senior person responsible for managing an area overall.
- Full scope SMCR firms will have to prepare and maintain a 'Management Responsibilities Map' ("**MRM**") showing the key roles within the firm, the people responsible for them, their responsibilities and lines of accountability. The PRA 'governance map' obligations remain the same (subject to an additional obligation to detail matters reserved to the governing body) and it will be renamed 'Management Responsibilities Map'.
- Full scope firms will be required to comply with New Handover Requirements requiring them to take all reasonable steps to ensure that a person taking on a senior manager role has all of the information and materials they could reasonably expect in order to do their job effectively. One means of achieving this is to require the outgoing senior manager to prepare a handover certificate, however this is not mandatory. Firms must have a policy in place explaining how they have complied with this requirement and keep adequate records of the steps they have taken. An internal handover policy and training for SM's will help firms to demonstrate reasonable steps.

## **Certification**

Firms are required to identify 'certified persons' who fulfil one or more specified 'Certification Functions' and certify anyone performing such a role as fit and proper at least annually. Firms will have 12 months to carry out the initial assessment and must certify by 10 December 2019.

## **Conduct Rules**

Firms must also ensure that employees comply with certain 'Conduct Rules' in respect of which firms will have notification training and record keeping obligations

## **Who will be a Senior Manager, who will be a Certified Person and who will be covered by the new Conduct Rules?**

### **Senior Managers: no territorial limit**

There is no territorial limit on the Senior Managers Regime. It will apply to anyone performing a Senior Management Function whether based in or outside the UK.

## **Certified Persons**

There are prescribed FCA and PRA Certification Functions ("**CFs**") in relation to which relevant individuals will need to be certified, including all individuals who have been designated as 'material risk takers' ("**MRTs**") for the purposes of the Solvency II Remuneration Code. Most current approved persons below senior management level will become Certified Persons ("**CPs**"). In addition some roles that are currently not subject to approval may require certification. Firms will be required to obtain regulatory references before appointing individuals to a CF but criminal records checks are not mandatory.

The PRA and FCA each specify different Certification Functions. The PRA CF's are as follows:

- Key Function Holders ("**KFHs**") at Solvency II firms; large NDF's and ISPV's (excluding PRA SMF's/NED's/FCA Controlled Function)
- Material risk takers at Solvency II firms and large NDF's
- Individuals who are managing a material risk taker

The FCA specifies eight CF's including a 'significant management' CF.

Firms must ensure that senior managers, non-executive directors (who are not senior managers) and certified persons are at all times fit and proper, and must certify them as such at least annually.

The Certification Regime will only apply to Certification Functions based in the UK or who spend more than 30 days a year in the UK or to individuals who are based outside the UK who are dealing with UK clients. Note however that all MRT's will be subject the Certification Regime wherever they are located.

## **Conduct Rules**

FCA Conduct Rules will apply to senior managers, certified persons, non SM directors (including NED's) and all employees except ancillary staff such as security, catering and cleaning staff. 'Employee' is broadly defined and includes contractors, temps and secondees.

The FCA Conduct Rules are comprised of Individual Conduct Rules applicable to all Conduct Rules staff and Senior Manager Conduct Rules. Both categories of Conduct Rules will apply to the firm's regulated and unregulated financial services activities (including related ancillary activities). This is a narrower application than the banking SMCR where the Conduct Rules apply to everything a person does.

The PRA's Conduct Rules apply to a smaller population: those holding PRA Certification Functions or performing an SMF on a temporary basis at Solvency II Firms, ISPV's and large NDF's.

Conduct Rules staff will have to be provided with training in relation to their application. Firm will be required to notify the regulators in the event Conduct Rule staff are subject to disciplinary action (written warning, suspension, dismissal or remuneration adjustment) for breaching the Conduct Rules.

## **Incoming EEA/Non EEA UK Branches**

The Certification Regime and Conduct Rules will only apply to people based in the UK; they will not extend to individuals outside the UK even if they deal with

UK clients. The Conduct Rules will only apply in relation to matters that are within the UK's scope of responsibilities.

A modified Senior Managers Regime will apply to EEA and non EEA Branches. EEA branches will have two SMF's (EEA branch Senior Manager and MLRO). Non EEA branches will have five FCA SMF's.

### **What is the streamlined SMCR and who does it apply to?**

Small NDF's (i.e. insurance firms that are out of scope of the Solvency II Directive and hold assets of £25m or less) are subject to the streamlined SMCR, which in broad terms is as follows:

- a shorter list of senior manager roles requiring FCA or PRA approval;
- a shorter list of prescribed responsibilities under the PRA's SIMR;
- more time to prepare scope of responsibilities documents;
- no requirement for a governance map;
- a shorter mandatory recordkeeping period for the scope of responsibilities;

Small run off firms will also be subject to a streamlined SMCR.

### **What preparatory steps should be taken?**

Firms that will be in scope need to consider:

- whether they come within the full or streamlined regime
- who should be on the implementation team
- how they will engage with senior managers (who are not currently SIMF's) and what processes they will adopt for agreeing statements of responsibility with senior managers
- how 'Certification' staff can be identified and certified annually
- how to ensure non-certified staff are not inadvertently performing certified functions
- which staff will be covered by the Conduct Rules and when
- how training should be updated and delivered
- what changes to employment documents and processes are required
- if changes to reference procedures and personal data retention are necessary
- what changes to recruitment processes, settlement agreements, handover and termination processes must be made
- which individuals will be covered in other group entities

- the practical implementation of the regime in relation to in-scope employees based overseas
- whether governance structures and arrangements need to be reviewed

Experience demonstrates the importance of engaging with senior managers early in the implementation process. Equally important is the provision of advice and assistance to them for example by producing a Senior Managers' Handbook and/or offering individual briefings.

### Timetable

What?	When?
FCA/PRA Consultations on insurance SMCR rules	26 July – 3 November 2017
PRA/FCA Policy Statements / Near Final Rules	4 July 2018
Firms to submit Approved Persons Conversion application documents to regulators	by 3 December 2018
Senior Managers and Certification Regimes will apply to insurers	10 December 2018
Requirement to certify certification function employees as fit and proper	10 December 2019
Application of Conduct Rules to "Other Conduct Rules Staff"	10 December 2019

This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

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