Individual accountability

The impact for financial services in Ireland

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01. Introduction

In recent years a number of regulators, including Ireland and the UK, have focused increasingly on individual accountability. Regulated firms are being required to identify senior managers, allocate responsibilities to these senior managers, draw together responsibility maps for the firm, and ensure that senior managers (and in some cases a wider range of staff) are fit and proper for their roles and meet the expectations of conduct rules established by the regulator. In July 2018 the Central Bank of Ireland put forward its proposals for a new Individual Accountability Framework which incorporates many of the elements introduced by the UK Senior Manager and Certification Regime. Legislation to facilitate the introduction of the new Framework is expected in Q2/Q3 2020.

Individual accountability is now a global concept and is becoming a regulatory focus area around the world – as, for example, in Australia (the Banking Executive Accountability Regime including the proposed Financial Accountability Regime), Hong Kong (the Manager-in-Charge regime), Ireland (proposed Individual Accountability Framework, including Senior Executive Accountability Regime and new Conduct Standards), Singapore (proposed guidelines on individual accountability and conduct), the UK (the Senior Managers and Certification Regime, the US (the latest guidance on the management of business lines and risk management), and in the Financial Stability Board's work on governance and misconduct. More countries are likely to follow suit over the coming years.

This increasing focus on individual accountability has been driven by three main factors. **First, to constrain excessive credit and market risk taking,** in particular by banks, through a focus on both heads of business lines and heads of control functions such as Compliance, Risk Management and Internal Audit.

Second, together with the greater emphasis on culture, to mitigate retail and wholesale misconduct risks through a focus on conduct standards and on senior managers taking reasonable steps to prevent regulatory breaches in the areas for which they are responsible. This is also part of a wider focus of both regulators and financial institutions to restore trust in the financial sector.

Third, to hold individual senior managers to account (including through lower remuneration and disciplinary actions) when regulatory breaches and other failures do occur.

Internationally, firms have taken the shift to greater individual accountability seriously, perhaps not least because of the potential consequences on individual senior managers of a failure to do so. In Ireland firms will need to undertake large-scale reviews and updates of governance structures, management reporting structures, individual responsibilities, governance maps, and management information.

02.
The potential Irish Regime

"Culture is set from the top down. It is a matter for boards and senior management, in the first instance, to set an effective culture that places the best interests of their customers first. Banks still have a distance to go to live up to their slogans of putting customers first."

Derville Rowland, Director General Financial Conduct, Central Bank of Ireland

On 24 July, the Irish Central Bank published the Behaviour and Culture Report into the five main Irish retail banks. The report was requested by the Minister for Finance under section 6A of the Central Bank Act 1942 at the end of 2017 as a result of the ongoing Tracker Mortgage Examination and was conducted in collaboration with the Dutch regulator, De Nederlandsche Bank ('DNB').

A series of culture reviews were undertaken in Ireland's retail banks which analysed:

- The leadership behaviours of the executive committee including the drivers of this behaviour in terms of group dynamics and mind-set; and
- The interplay between the executive committee and relevant internal stakeholders in the context of strategic decision-making.

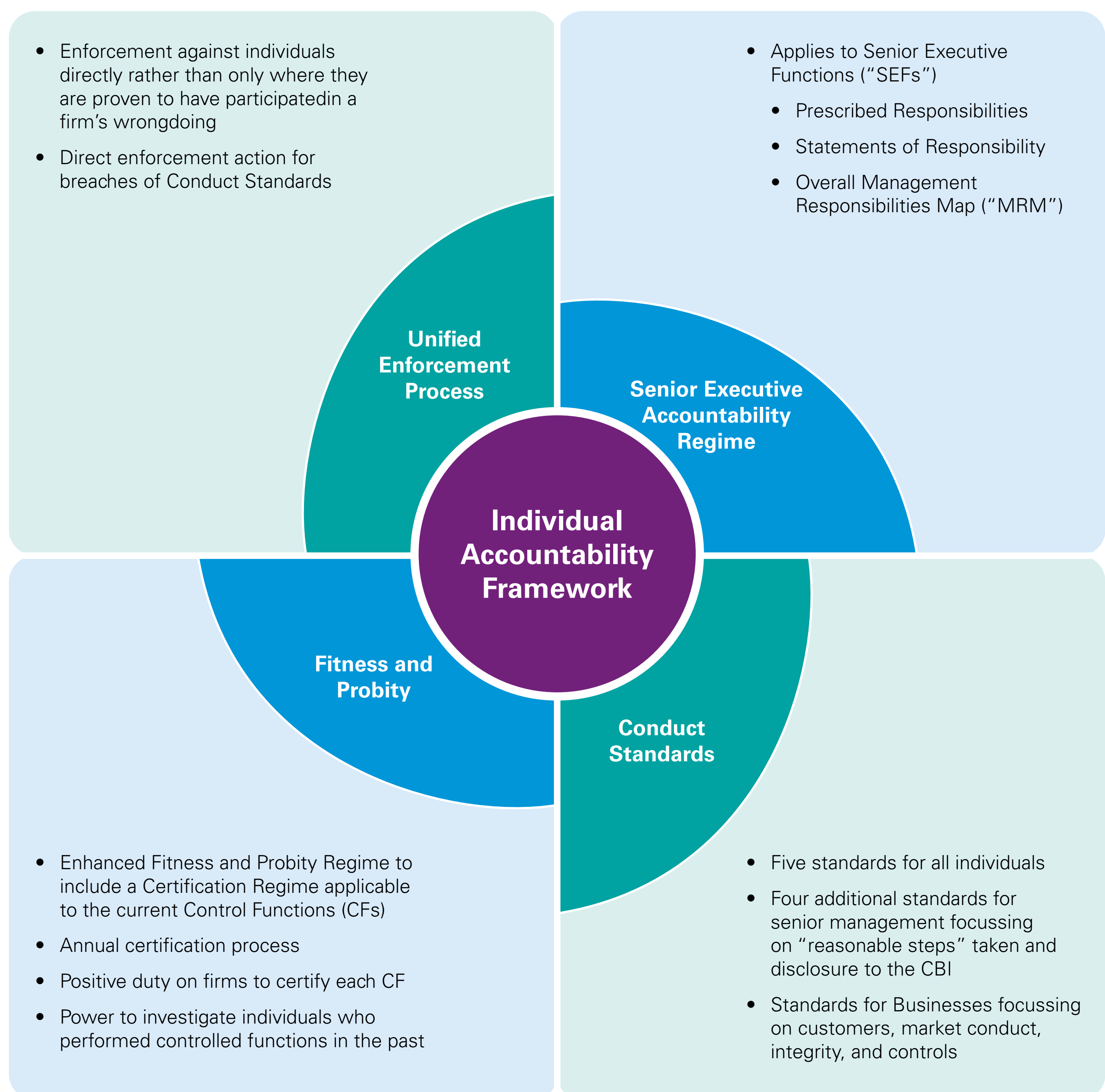
As part of its report the Central Bank has recommended that that legislation be introduced by Government to facilitate the introduction of an Individual Accountability Framework referred to as the "Senior Executive Accountability Regime" and a Consultation Paper is expected imminently. This new accountability framework, would apply to banks and other regulated financial services providers and would go significantly beyond the current requirements for staff to be fit and proper, setting conduct standards for staff and ensuring clearer lines of accountability within firms.

The proposed Individual Accountability Framework will serve as a toolkit for the Central Bank comprising various methods by which to promote the desired culture of compliance in financial services firms. This Individual Accountability Framework will be consisted of:

- **Conduct Standards:** Standards of behaviour for regulated financial services providers and the individuals working within them (the Conduct Standards);
- **A Senior Executive Accountability Regime (SEAR),** which will be designed to ensure clearer accountability;
- **Enhancements to the existing Fitness and Probity Regime;** and
- **A unified enforcement process.**

The CBI's proposals for an Individual Accountability Framework

The Senior Executive Accountability Regime (SEAR) is one of four elements proposed in the CBI's July 2018 report Behaviour and Culture in Irish Retail Banks:



Legislation to introduce these requirements is expected in Q2/Q3 2020

Conduct Standards

While certain conduct standards are already embedded in the current regulatory framework in the form of the Consumer Protection Code and the Fitness and Probity Regime, the Central Bank has proposed enhancing these with the introduction of three new sets of standards:

- Common Conduct Standards for all staff in regulated financial services providers;
- Additional Conduct Standards for senior management, which will apply to staff currently in Pre-Approval Controlled functions (PCF);
- Standards for Business, i.e. common standards which will be applicable to firms across the regulated financial services sector.

Senior Executive Accountability Regime

A key recommendation arising from the Central Bank's report is the introduction of a Senior Executive Accountability Regime. The Central Bank envisages this regime applying in the first instance to:

- Credit institutions (excluding credit unions);
- Insurance undertakings (excluding reinsurance undertakings, captive (re)insurance undertakings and Insurance Special Purpose Vehicles);
- Investment firms which underwrite on a firm commitment basis and/or deal on own account and/or are authorised to hold client monies/assets; and
- Third country branches of the above.

The regime will introduce Senior Executive Functions (SEFs) including board members, executives reporting directly to the board and heads of critical business areas. The Central Bank has indicated that it will at least map to the PCF roles under the current Fitness and Probity Regime under the Central Bank Reform Act 2010 (CBRA). The current indication is that while some SEFs may be mandatory, the Central Bank intends to allow for a degree of flexibility in terms of how firms structure their senior management team.

Each SEF will have prescribed responsibilities which will be proposed by the Central Bank in order to ensure that there is an SEF responsible for all key conduct and prudential risks relevant to each firm. Additionally, and in line with the current UK Senior Managers Regime, SEFs will be required to prepare a Statement of Responsibilities documenting their role and areas of responsibilities, and firms will be required to produce Management Responsibilities Maps documenting key management and governance arrangements. This will include reporting lines outside of the in-scope legal entity as well as group governance arrangements where relevant.

Enhancements to Fitness and Probity Regime

The Central Bank has proposed supplementing the existing Fitness and Probity (F&P) Regime with the introduction of a certification regime for those currently occupying Control Functions (CFs). The new regime would oblige firms to certify on an annual basis that the individuals in question are fit and proper persons to perform their functions. The Central Bank is also seeking the implementation of its previous recommendation to publish refusals of appointments to PCF roles and to investigate those who performed PCF roles in the past.

Unified Enforcement Process

Under current enforcement rules, the Central Bank may only pursue action against an individual where that individual is a 'person concerned in the management' of the firm and where the case has been proven against the firm and it can be proven that the individual participated in the breach. The Central Bank is seeking to remove these hurdles in order to pursue individuals directly for their misconduct.

The current Fitness and Probity Regime

In April 2019, the CBI issued a 'Dear CEO' letter which stated that firms lacked general awareness of their own legal obligations under the current F&P regime. It noted that it had taken enforcement actions for failures to establish and/or follow proper systems and controls to ensure compliance with the F&P regime. Specifically, it focused on the following areas of non-compliance by firms:

- **Failure to provide for the ongoing nature of the obligations under S.21 of the CBRA.**
  Firms are required to conduct due diligence on an ongoing basis to ensure that employees performing CFs comply with the F&P standards required of them. This is particularly important where, once appointed to a CF role, the F&P regime does not provide for ongoing fitness and probity monitoring by the CBI;

- **Failure to report issues to the CBI.**
  The CBI has recorded instances where firms have identified fitness and probity concerns about an individual, and despite taking steps to address these, have failed to report these concerns to the CBI. This then impacts the CBI's ability to consider individual misconduct, particularly in respect of future PCF applications;

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- **Failure to seek pre-approval from the CBI prior to appointing individuals to PCF roles.**
  This approval process incorporates a fitness and probity assessment by the CBI of the proposed PCF role holder. Although this applies to the proposed appointee, the CBI has reiterated that the statutory obligation is on the appointing firm to seek approval before appointment; and
- **Failure to conduct adequate due diligence for senior positions (i.e., PCF roles).**
  PCF applicants are required to complete an Individual Questionnaire (IQ) which the CBI considers prior to approval. However, the CBI has noted that some applicants have failed to disclose material facts which were either known to proposing firms, or would have been detected with proper due diligence by firms. This is of particular concern where the IQ contains a declaration by the firm confirming the suitability of the candidate and that all due diligence has been conducted.

This 'Dear CEO' letter also referenced enforcement actions which sanctioned firms for failing to establish and/or follow proper systems and controls to ensure compliance with the F&P regime. The public statements in respect of these actions reinforce the previous points made by the CBI. In these cases, firms were sanctioned for non-compliance such as not conducting adequate due diligence on CF/PCF appointees; failing to take reasonable steps to ensure that CF and PCF applicants agreed to and complied with the F&P standards; and establishing proper systems and procedures to ensure compliance with the firm's obligations under s.21 of the CBRA.

The CBI has also reinforced its 'gatekeeper' role, which empowers it to refuse to appoint candidates to PCF roles where it has concerns on their fitness and probity. Firms have increasingly withdrawn candidates from the PCF process where they have become aware that the CBI has concerns with the potential PCF appointee. As at October 2019, over 80 applications for senior positions were withdrawn where the Central Bank had challenged the applicant. This is in addition to four outright refusals.

The CBI has also recently conducted on-site inspections of firms' F&P policies and procedures. The findings from these inspections will undoubtedly inform the shape and focus of the Individual Accountability Framework for Ireland.

Implications for Irish financial services firms

As noted above, the CBI has clearly articulated the deficiencies in firms' compliance with the existing F&P regime, including firms' lack of understanding of their current obligations. The introduction of an Individual Accountability Framework will present several additional challenges for Irish financial services firms both to address current gaps and also to transform existing operations and structures to embed the changes brought by the new requirements.

Firms will need to clearly understand their obligations under the new Framework. This will involve some interpretation of prescribed responsibilities and also of any principle-based standards, in particular, the new Conduct Standards. The new regime will also present a number of operational challenges, particularly in relation to the formulation of Responsibility Maps and individual statements of responsibility as well as the ongoing maintenance of documentation and the need to meet training needs for staff as a result of the new rules.

Central Bank of Ireland: PCF roles under the current Fitness and Probity Regime

Pre-Approval Controlled functions (PCFs)

General

PCF–1 Executive Director
PCF–2 Non–executive director
PCF–3 Chairman of the board
PCF–4 Chairman of the audit committee
PCF–5 Chairman of the risk committee
PCF–6 Chairman of the remuneration committee
PCF–7 Chairman of the nomination committee
PCF–8 Chief Executive
PCF–9 Member of partnership
PCF–10 Sole Trader
PCF–11 Head of Finance
PCF–12 Head of Compliance
PCF–13 Head of Internal Audit
PCF–14 Chief Risk Officer
PCF–15 Head of Compliance with responsibility for Anti-Money Laundering and Counter Terrorist Financing Legislation
PCF–16 Branch Manager of branches in other EEA countries
PCF–17 Head of Retail Sales
PCF–42 Chief Operating Officer

Insurance

PCF–18 Head of Underwriting
PCF–19 Head of Investment
PCF–43 Head of Claims
PCF–48 Head of Actuarial Function

Banking

PCF–21 Head of Treasury
PCF–22 Head of Credit
PCF–23 Head of Asset and Liability Management

Stock Exchange

PCF–24 Head of Traded Markets
PCF–25 Head of International Primary Markets
PCF–26 Head of Regulation
PCF–27 Head of Operations

Investment Firms

PCF–28 Branch Managers in Ireland
PCF–29 Head of Trading
PCF–30 Chief Investment Officer
PCF–31 Head of Investment
PCF–45 Head of Client Asset Oversight

Investment Intermediaries/Collective Investment Schemes

PCF–32 Branch Managers in Ireland
PCF–33 Head of Transfer Agency
PCF–34 Head of Accounting (Valuations)
PCF–35 Head of Trustee Services
PCF–36 Head of Custody Services

UCITS Self-Managed Investment Company/ Management Company

PCF–37 Head of Transfer Agency
PCF–38 Head of Accounting Valuation
PCF–39 Designated Person to whom a director of a UCITS Self Managed Investment Company or Non UCITS Self Managed Investment Company or Management Company may delegate the performance of the management functions
PCF–46 Head of Investor Money Oversight

Payment Institutions

PCF–40 Branch Managers within the State

Retail Credit Firms

PCF–47 Head of Credit

Financial Service Providers established outside Ireland

PCF–41 Manager of a branch in Ireland of a regulated financial service provider established in a country that is not an EEA country

Individuals undertaking these roles must:

1. Be assessed as being fit and proper for the role by the financial institution.
2. Be approved by the regulator to undertake the specific role in a specific financial institution (the approval does not carry across to other roles or to other financial institutions). This approval may be granted on the basis of a review of the application forms alone, or the regulator may supplement this with one or more interviews of a candidate.
3. Comply with the CBI's Fitness and Probity standards on an ongoing basis.

UK Financial Conduct Authority (FCA) and Prudential Regulatory Authority (PRA): Senior Manager Functions under the current Senior Manager and Certification Regime

Senior Manager Roles covered by the SMCR for banks, building societies and PRA designated investment firms.

PRA population of senior managers	FCA population of senior managers (in addition to the PRA population)
SMF–1 Chief Executive	SMF–3 Executive Director
SMF–2 Chief Finance Function	SMF–13 Chair of the Nomination Committee
SMF–4 Chief Risk Function	SMF–16 Compliance Oversight
SMF–5 Head of Internal Audit	SMF–17 Money Laundering Reporting
SMF–6 Head of Key Business Area	SMF–18 Other Overall Responsibility
SMF–7 Group Entity Senior Manager	SMF–21 EEA Branch Senior Manager
SMF–9 Chair of the Governing Body	SMF–22 Other Local Responsibility Function (Non-EEA Branch)
SMF–10 Chair of the Risk Committee	SMF–27 Partner
SMF–11 Chair of the Audit Committee	
SMF–12 Chair of the Remuneration Committee	
SMF–14 Senior Independent Director	
SMF–24 Chief Operations Officer	

Senior Manager Roles covered by the SMCR for Insurers

PRA population of senior managers	FCA population of senior managers (in addition to the PRA population)
SMF–1 Chief Executive	SMF–3 Executive Director
SMF–2 Chief Finance Function	SMF–13 Chair of the Nomination Committee
SMF–4 Chief Risk Function	SMF–15 Chair of the With-Profits Committee
SMF–5 Head of Internal Audit	SMF–16 Compliance Oversight
SMF–6 Head of Key Business Area	SMF–17 Money Laundering Reporting
SMF–7 Group Entity Senior Manager	SMF–18 Other Overall Responsibility
SMF–9 Chair of the Governing Body	SMF–22 Other Local Responsibility Function (Non-EEA Branch)
SMF–10 Chair of the Risk Committee	SMF–23b Conduct Risk Oversight
SMF–11 Chair of the Audit Committee	SMF–27 Partner Function (Lloyds only)
SMF–12 Chair of the Remuneration Committee	
SMF–14 Senior Independent Director	
SMF–20 Chief Actuary	
SMF–20a With–Profits Actuary	
SMF–21 EEA Branch Senior Manager	
SMF–23 Chief Underwriting Officer	
SMF–23a Underwriting Risk Oversight Function (Lloyds only)	
SMF–24 Chief Operations Officer	
SMF–25 Small Insurer Senior Management Function	
SMF–26 Head of small run–off firm	

Senior Manager Roles covered by the SMCR for FCA-solo regulated firms*

SMF–1 Chief Executive	SMF–13 Chair of the Nominations Committee
SMF–2 Chief Finance Function	SMF–14 Senior Independent Director
SMF–3 Executive Director	SMF–16 Compliance Oversight
SMF–4 Chief Risk Function	SMF–17 Money Laundering Reporting Officer
SMF–5 Head of Internal Audit	SMF–18 Other Overall Responsibility
SMF–7 Group Entity Senior Manager	SMF–19 Head of Third Country ranch
SMF–9 Chair of the Governing Body	SMF–21 EEA Branch Senior Manager
SMF–10 Chair of the Risk Committee	SMF–24 Chief Operations Function
SMF–11 Chair of the Audit Committee	SMF–27 Partner
SMF–12 Chair of the Remuneration Committee	SMF–29 Limited Scope Function

*Allocation of SMFs for FCA-solo regulated firms depends on whether the Firm is Enhanced, Core or Limited Scope

Individuals undertaking these roles must:

1. Be assessed as being fit and proper for the role by the financial institution.
2. Be approved by the regulator(s) to undertake the specific role in a specific financial institution (the approval does not carry across to other roles or to other financial institutions). This approval may be granted on the basis of a review of the application forms alone, or the regulator(s) may supplement this with one or more interviews of a candidate.
3. Have clear and succinct individual statements of responsibilities. This should include, but not be confined to, an assignment of the "prescribed responsibilities" listed by the regulators. In addition, the financial institution should develop a comprehensive and up to date overall "management responsibilities map" that shows how all the individual responsibilities fit together, together with reporting lines and committee structures (indeed, one of the prescribed responsibilities that has to be allocated to a senior manager is the responsibility for maintaining this mapping. Note: some firms do not need to assign prescribed responsibilities or create "management responsibilities maps" depending on their status under SMCR.
4. Meet the Conduct Rules for senior managers and for all non-ancillary staff. In particular, senior managers are required to take "reasonable steps" to ensure that the business of the firm for which they are responsible is controlled effectively and complies with relevant requirements and standards of the regulatory system. What is "reasonable" will depend on the specific facts of any particular situation, but a senior manager must be able to satisfy the regulator that they took "reasonable steps" to avoid any regulatory breach occurring in their area of responsibility.

Applying the UK SMCR standard, the below evidence may be required to substantiate compliance with the regime

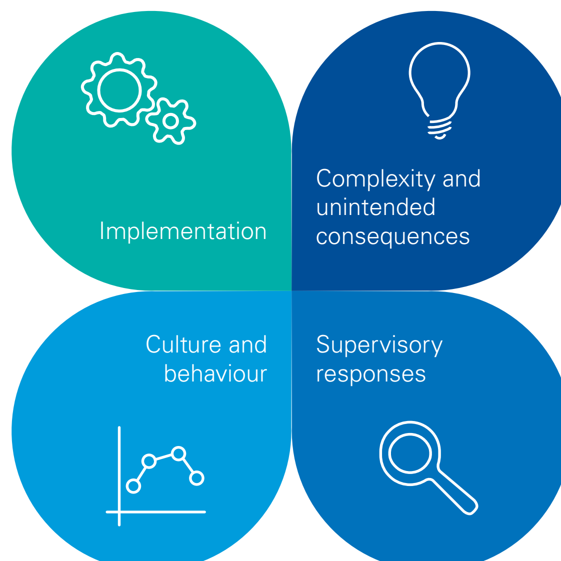
Potential evidence to meet the "reasonable steps" test

Structure	Execution	Information	Non-executive directors
Governance framework	Systems and controls in place	Management information	Challenge of the executive
Policies and procedures	Appropriate delegations	Regular reporting	Forward looking and proactive approach
Reporting lines	Active management	Minutes of meetings	Regular and effective meetings of the board and board committees
Committee memberships	Proactive participation in committees	Incident/breach escalation	Competent and active members of the board and board committees
		Regulatory correspondence and meetings/interviews	Sufficient management information to assess risks and significant business activities

03. Experience with the UK regime

The UK's SMCR has a significant impact on financial institutions' governance frameworks, and to some extent on their culture and behaviours. Some implementation issues have arisen, in particular in more complex groups and the UK subsidiaries of overseas banks and insurers. Supervisory attention has focused primarily on the approval of senior managers, and on checking that financial institutions have the main elements of the regime in place.

We focus in this chapter on the experiences of UK financial institutions with the implementation of the SMCR, including the extension of the Senior Insurance Managers Regime ("SIMR") This covers how they have approached the implementation challenge, what has changed in terms of culture and behaviours, the main issues arising, and the focus of supervisors. Some lessons emerge for the introduction of similar regimes in other countries.



Implementation

Firms have taken a wide range of approaches to implementing the SMCR.

At a minimum, some have simply "ticked the boxes" by producing sets of individual responsibilities for senior managers and an overall mapping of governance arrangements, not least because these components are essential for gaining approvals for candidates for senior manager roles. Such firms are more likely to find that they have not allocated responsibilities with sufficient clarity or to sufficiently senior managers, have not focused sufficiently on what each senior manager is actually responsible for, have not covered all relevant business functions and activities, and have not provided sufficient information on governance arrangements (including reporting lines and committee structures and memberships).

In most cases, however, firms have gone beyond this and engaged more with the spirit of the new regime. The duty of responsibility on senior managers may have been particularly important in concentrating minds here. Firms at this more active end of the spectrum have taken the opportunity to review their governance arrangements, and to clarify and refresh roles and responsibilities, management information, reporting and escalation routes. These firms have followed some combination of:

- Established SMCR programmes with clear leadership and buy-in from the Chair and CEO. Senior leadership has been fundamental in driving willing adoption and adherence.
- Allocated ownership across a number of key functions with clear roles and responsibilities for meeting each element of the new regime.
- Undertaken a gap analysis of their current state against the SMCR requirements.
- Reviewed their current allocation of responsibilities. In most cases this has led to changes in allocation and to a general "cleaning up" and updating of responsibilities, and in some cases to more streamlined and more effective management.
- Reviewed governance structures, including senior manager structures, board and executive committee terms of reference and memberships, and individual and committee reporting lines. This has led to an overhaul of the governance framework in some firms.
- Developed a "reasonable steps" framework to assist in evidencing that senior managers have taken reasonable steps to avoid regulatory breaches.
- Reviewed management information to assist senior managers in discharging their responsibilities. Some firms have overhauled their risk management system as it became clear that management information was inadequate and did not enable some senior managers to gain assurance that necessary systems and controls were in place and were working effectively.
- Enhanced the training and development of current and candidate senior management (including board members), including on the nature and objectives of the SMCR.
- Established quality assurance reviews of programme deliverables (for example statements of responsibilities, reasonable steps framework and the firm' s conduct breach methodology).
- Engaged proactively with regulators.

Successful programmes have usually been based on a willingness to use the SMCR as an opportunity to reassess the appropriateness and effectiveness of current governance arrangements and to challenge the roles of both individuals and committees. This has facilitated improved governance, and in some cases enabled a degree of rationalisation and simplifcation of governance structures. However, some firms found that because this re-engineering was poorly managed or thought through it resulted in arrangements that were not fit for purpose or were overly complicated or burdensome, requiring further re-working to create an effective and efficient governance framework.

Successful programmes have also usually leveraged templates and documentation that were already in place and sought to align new processes and procedures with existing practices and IT systems, and recognised competing priorities, dependencies (for example with some elements of MiFID 2 and Solvency 2) and stress points.

New entrants to the UK market (subsidiaries and branches of overseas parents, and new UK-headquartered challenger firms) have engaged with the SMCR and generally understood the importance of governance framework design and of allocating responsibilities to appropriate individuals, taking into consideration proposed reporting lines and overall responsibility for certain functions and business lines. In some cases this has had an impact on recruitment decisions (for example whether to hire someone with an understanding of the regime and the necessary skills and expertise to discharge their responsibilities appropriately), and on the allocation of responsibilities and reporting lines between the subsidiary or branch and its parent.

One key implementation challenge that has emerged relates to the ownership of the regime and the transition from implementation to business as usual. At the implementation stage, and for the business as usual operation of the senior managers element of the new regime, most firms have allocated ownership to the CEO's office. For the business as usual operation of the Certification Regime, firms have allocated ownership more evenly between the COO/CEO office, Compliance and HR. Some firms have underestimated the operational resources required to establish and operate a Certification Regime.

The importance of HR, and of an effective working relationship between HR and a firm' s control functions, has become clearer in firms with a large number of certified persons, where the firm will be responsible for assessing their fitness and propriety on an annual basis, and for conducting enhanced checks at the recruitment stage. Some firms have introduced technology to facilitate data collection, reporting and record keeping in this area. HR functions in some firms are challenging themselves on whether they have the right skills and capabilities to run these regimes on a business as usual basis.

Culture and behaviour

Given the timescales required to achieve significant and tangible cultural change, the jury is still out on the extent to which the SMCR has driven large scale changes in culture. However, there are clearer indications that the regimes have led to improved governance in many banks and insurers.

Senior managers have reviewed and challenged their own personal responsibilities and considered whether these are appropriate. Even where the SMCR largely codified existing responsibilities, a much brighter spotlight has been targeted on senior manager accountability. Senior managers have become wary of the possible sanctions on them for regulatory breaches in their areas of responsibility, and this has promoted greater control and scrutiny over their respective areas. But, as a result, senior managers have become more empowered by this clarification of accountability and delineation of responsibilities.

Similarly, there have been reports that senior managers have become more involved at board, board committee and executive committee meetings, with more active participation and discussion. The downsides of this may be (a) a corresponding decision-making paralysis at lower levels, with lower level management becoming more reluctant to make decisions themselves and escalating more to senior managers and to senior manager level committees; and (b) committees becoming an advisory panel for the (senior manager) chair of the committee.

Some firms have linked to some extent the SMCR with other initiatives on culture, values and behaviours. Conduct risk has become better integrated within the overall risk framework, and training on conduct has become more of a business as usual activity than it used to be.

Complexity and unintended consequences

Firms have struggled with the implementation of the SMCR in five key areas.

First, some firms and senior managers have found it difficult to understand fully their obligations in a number of areas. Many firms have found it difficult to define how far they – and their senior managers – should go to establish that "reasonable steps" have been taken to avoid regulatory breaches, and the extent to which second and third line of defence control functions and internal audit should be involved in monitoring this and providing assurance that the appropriate steps have been taken.

Firms have also struggled with how to interpret some of the prescribed responsibilities such as those relating to culture; with the identification and notification (internally, and to the regulators) of breaches of the Conduct Rules; and – for the banks, building societies and major investment firms so far subject to the Certification Regime – with the identification of populations for the Certification Regime (including the interpretation of "significant harm" and the extent to which roles requiring formal qualifications should be captured).

A more recent challenge here relates to the roles and responsibilities of a firm' s chief of operations, not least in the context of the many issues for firms emerging from fintech, operational continuity, legacy IT systems and cyber security.

Second, some firms have found it difficult to establish the identification and role of group entity senior managers and the application of the "other overall responsibility" senior manager function. Some banks and insurers with overseas parents have struggled to identify and to allocate a clear set of responsibilities to group level senior managers (including not just business managers, but also in cases where risk and compliance functions are provided in part at parent level), and to define how responsibilities will be shared with UK-based senior managers within a matrix management structure.

In some cases an overseas parent has been reluctant to designate managers based outside the UK as senior managers, even if they meet the significant influence test. In other cases this has led to a multiplicity of designated senior managers at both parent and subsidiary/branch levels, which can seem disproportionate to the size of the subsidiary/ branch. Further complexity has arisen where an overseas parent operates through both a subsidiary and a branch in the UK, with some senior managers undertaking senior management functions in both UK entities.

Even within the UK, issues have arisen where individuals in an unregulated group entity have a significant influence over one or more regulated entities within the group.

Firms are also often unclear about how many senior managers should be allocated to the group entity senior manager function – some firms may have identified too many senior managers to this function, and in some cases have identified managers who are too junior (in both cases this blurs accountability).

Third, firms have faced a series of operational challenges, such as resourcing issues, particularly in Compliance and HR functions; the cost associated with tailored training for different cohorts of senior management and certification regime staff; preparing and maintaining documentation, and ensuring consistency between the management responsibilities map and individual statements of responsibilities; communicating the change in an effective way across the entire organisation; and obtaining and providing regulatory references.

Fourth, where branches of European banks are reauthorising as non-EEA branches this has resulted in these branches having to apply the non-EEA Branch SMCR regime, which captures a wider range of senior manager roles and is not specifically designed with some of the smaller European branches in mind.

Finally, some firms have struggled to implement the SMCR at the same time as introducing organisational change as a result of other regulatory requirements (recovery planning, resolution and the ringfencing of retail banks), Brexit, mergers and acquisitions, or other group restructurings.

Supervisory responses

During the transition period in 2016 most of the supervisory scrutiny was on larger banks, investment firms and insurers, many of which were asked to make changes to the designation of senior manager roles, statements of individual responsibilities, and the management responsibilities map. Smaller banks and insurers were generally left to implement the SMCR without the same level of scrutiny, except where supervisors were engaged with the firm in other areas, where there were obvious issues in implementation, or where new candidates were nominated for senior manager roles.

On a more steady state basis, supervisors will usually review individual statements of responsibilities and the firm' s management responsibilities map in preparation for meetings with senior management. Supervisors may also use meetings with senior managers to test how well the SMCR has been embedded. This may highlight inadequacies that need to be addressed.

For example, in some cases management responsibility maps have been criticised by supervisors for being too complex and unwieldy, making them not only hard to navigate but also difficult to maintain as live documents. In other cases firms have been requested to provide more detail in management responsibility maps on governance arrangements, particularly their interactions with parent firms and group arrangements more generally (for example where senior executive remuneration is determined by a group-level remuneration committee, or where IT and other infrastructure issues are owned and managed at group level).

Supervisors have also sometimes asked for additional rationale for allocations of responsibilities that do not appear to be 'standard'.

Other areas in which supervisors have expressed an interest include:

- challenging firms where senior manager roles have not been allocated to the most senior relevant individual in the firm (the supervisors refer to this as 'juniorisation');
- challenging firms where global heads based in the UK have not been designated to be senior managers;
- requesting information on Certification arrangements, and even requesting firms to undertake an internal audit on their application of the Certification Regime;
- indicating concern where responsibility for financial crime has been allocated to a money laundering reporting officer who is not of sufficient seniority, or has been split across individuals; and
- requesting that firms present information about the way in which different entities might be linked from a governance perspective (especially in the event of matrix management, where individuals have dotted reporting lines into other entities).

The PRA and FCA also now have much greater insight and clarity on regulatory breaches as a result of the reporting and notification requirements in the SMCR. These data are likely to inform future supervisory and thematic activity across firms and sectors.

Finally, the SMCR is likely to be reinforced over time through enforcement actions against senior managers. For example, the FCA's May 2018 enforcement notice against the CEO of a major UK banking group made specific reference to the role of a CEO within the SMCR and to Individual Conduct Rule 2 (acting with due skill, care and diligence).

Preparing for the Irish regime

Based on the UK experience, the CBI's Individual Accountability Framework will have significant impacts for Irish firms. Firms will need to consider how to resource both the initial implementation of the CBI requirements, as well as transitioning to the business as usual environment and ongoing maintenance. Governance arrangements will need to be clarified (including Board composition and reporting), as well as training requirements, impacts on the HR function, management information and technology. All of these bring several operational challenges which will need to be addressed effectively to embed the CBI requirements throughout all levels and functions within the organisation.

Although the legislation is not expected until Q2/Q3 2020, there are several practical steps that firms can take to get ready now.

- If not already done, in-scope firms should communicate the pending introduction of the regime across the organisation, especially to the senior management team. It should also be on the Board agenda;
- Firms should consider who will be responsible both for implementation of the SEAR and ongoing compliance. This should include identifying the Sponsoring Executive for the implementation, which should be a senior executive such as the CEO/COO;
- Firms should review current governance structures and organisational design of senior management team: including terms of reference for committee structures as well as roles on each committee, job descriptions/role profiles and RACI / delegated authorities matrices;
- HR processes and activites across the end to end employee lifecycle should be mapped. This includes, but is not limited to, those such as recruitment assessment and onboarding, succession management, learning and induction, exits/handovers/ references, remuneration policies, and conduct and breach management;
- The relevant documentation, policies, procedures, and reviews should be considered. For example, firm value statements may need revisiting in the light of the proposed conduct standards; and
- Finally, firms should consider the results of any reviews already undertaken which indicate deficiencies in the control environment, whether cultural issues or otherwise.

The CBI has been clear that firms are expected to comply with not just the letter, but also the spirit of the new requirements. Successful implementation should not only clarify accountabilities but also drive positive cultural change throughout the organisation; strengthening the tone and ownership from the top, creating a culture of challenge, escalation as well as improving the level of detail, clarity and quality of conversations on culture and expected behaviours.

05. The wider international context

Other countries are also introducing measures to reinforce individual accountability for senior managers, and in some cases codes of conduct applicable to a wider range of staff. These measures are broadly similar to the UK SMCR, although the details vary across countries. In addition, the Financial Stability Board (FSB) has highlighted the importance of individual responsibility and accountability in a recent paper on strengthening governance frameworks to mitigate misconduct risk. The following diagram outlines the key initiatives in place today.

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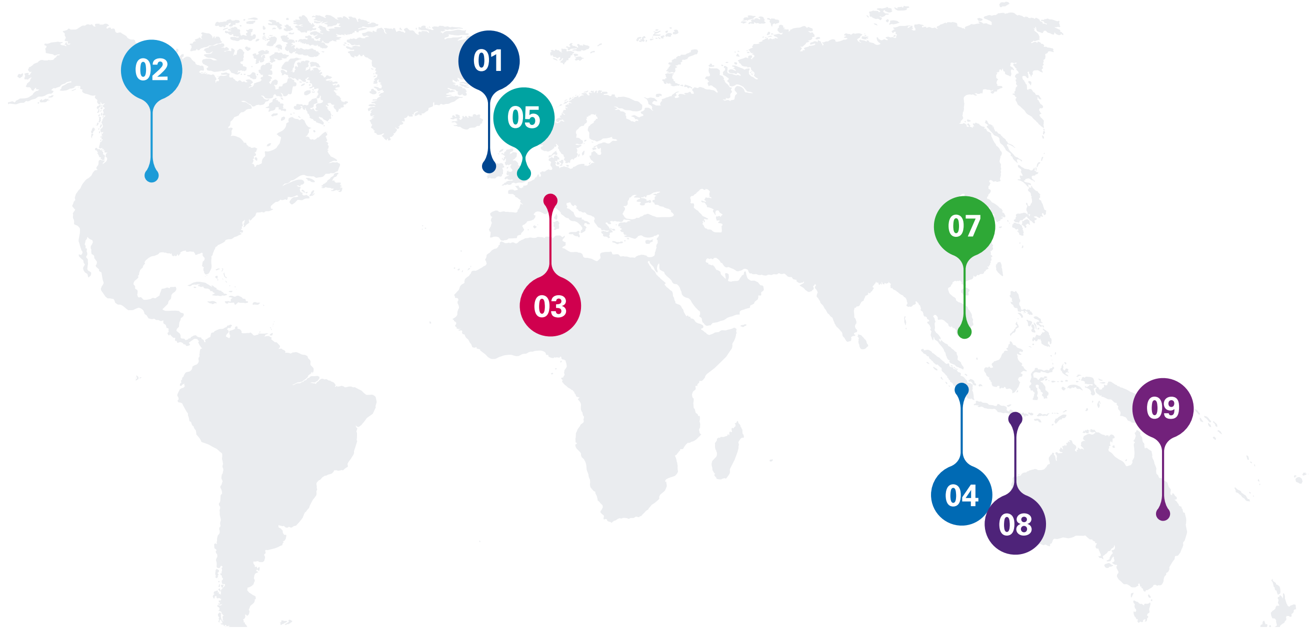

01 – Ireland

- July 2018 – CBI proposed the introduction of an 'Individual Accountability Framework' including:
  - A Senior Executive Accountability Regime (SEAR);
  - A set of Conduct Standards;
  - An enhanced Fitness and Probity Regime, including a Certification Regime;
  - A unified enforcement process.

There is no indication that these proposals have changed. Introductory legislation has been postponed, with further delays expected. Likely introduction of legislation in Q2/Q3 2020.

02 – USA

- January 2020 – Federal Reserve proposed supervisory guidance on management of business lines and independent risk management and controls for large financial institutions: no change registered, possibly associated with broader enforceability considerations.
- July 2020 - U.S. Securities and Exchange Commission (SEC) Regulation Best Interest, addressing broker-dealer standards of conduct, will come into effect
- Although ethics and compliance considerations are regularly prevalent, with corrective action taken against individuals for misconduct, no further activity by banking regulators has been noted.

03 – FSB

- April 2018 – FSB published a 'toolkit' to strengthen governance frameworks to mitigate misconduct risk in both retail and wholesale markets.
- The 'toolkit' supplemented earlier FSB work on risk governance, remuneration, benchmark setting and culture.

04 – Malaysia

- February 2018 – The Central Bank of Malaysia released a discussion paper on proposals for responsibilities mapping for senior roles.

05 – UK

- March 2016 – Introduction of Senior Managers & Certification Regime (SMCR) (for Banks only).
- December 2018 – SMCR was extended to Insurers from the existing Senior Insurance Managers Regime (SIMR).
- December 2019 – SMCR was extended to all solo regulated firms.

06 – European Commission

- October 2019 – European Commission published consultation on addressing issues relating to the 'fit and proper' regime for key function holders under CRD IV.
- The Commission is considering a potential expansion of the role of national regulatory authorities in 'fit and proper' assessments.

07 – Hong Kong

- Manager-in-Charge (MIC) Regime was introduced in Hong Kong in 2017.

08 – Singapore

- April 2018 – Monetary Authority of Singapore proposed Guidelines on Individual Accountability and Conduct.

09 – Australia

- January 2020 - Financial Accountability Regime (FAR) draft proposal paper published regarding an extension of the existing Australian Prudential Regulation Authority (APRA) Banking Executive Accountability Regime (BEAR) to include all APRA regulated entities and solely Australian Securities and Investment Commission (ASIC) regulated entities. The prosed FAR will be jointly administered by APRA and ASIC.

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06. How KPMG can help

KPMG's Risk and Regulatory Consulting team comprise of experts in Fitness & Probity, Conduct Risk, UK SMCR and Australian BEAR specialists who have assisted clients in the design and implementation of individual accountability regimes in the UK and Australia.

Our team has unparalleled experience in financial services risk and regulation and can help you understand your requirements, how to practically implement these changes into your existing business model in order to ensure the requirements are properly embedded and remain fit for purpose.

Members of our team having worked in the UK and Australia, both with the regulators and firms, have a deep understanding of the SMCR and BEAR. They have worked with a range of banks, building societies, major investment firms and insurers to support the design and implementation of individual accountability readiness programmes, and to identify and address the typical challenges/issues that arise across governance, people, process and technology.

1. Programme Management

- End to End programme management
- Multi-disciplinary team across Regulatory, Risk, Legal, IT, People & Change
- Change management design and implementation
- Target Operating Model design and implementation

2. Design and implementation

- Linking accountability regime implementation to wider initiatives such as governance effectiveness and cultural change
- Drafting role profiles and individual statements of responsibility
- Developing management responsibilities maps and ensuring overall consistency
- Formulating individual responsibility policies and procedures
- Conduct Rules training and awareness
- Development and implementation of technology solutions to aid compliance
- Preparations for senior manager approval interviews, handover meetings, files and induction
- Record keeping

3. Reasonable steps

- Review and design of frameworks to support senior managers taking reasonable steps to avoid regulatory breaches
- Workshops to review, implement and embed a reasonable steps approach
- Gap analysis against regulatory expectations and peers
- Conducting 'scenario analysis' testing to ensure the outcomes are effective and as intended
- Continuing reasonable steps assurance

4. Assurance

- Conducting a gap analysis against regulatory requirements and industry standards
- Review of policies and procedures – for both implementation and business as usual
- Internal audit support
- Business as usual operational effectiveness reviews, including board effectiveness reviews
- Conducting Governance Framework assessments in line with the overarching management responsibilities maps
- Review and implement control environment frameworks to support Senior Managers accountabilities

5. Remediation

- Providing support to deliver requirements following feedback from supervisors
- Providing support to deliver requirements from the outcomes of post-implementation internal audit reviews or other external assurance reviews (including Supervisory Risk Mitigation Programmes)

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