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Response to FCA CP25/21: Senior Managers & Certification Regime Review

About the Building Societies Association

The Building Societies Association (BSA) represents all 42 UK building societies, including both mutual-owned banks, as well as 7 of the largest credit unions. Building societies have total assets of almost £525 billion and, together with their subsidiaries, hold residential mortgages of over £395 billion, 24% of the total outstanding in the UK. They also hold £399 billion of retail deposits, accounting for 19% of all such deposits in the UK. Building societies account for 40% of all cash ISA balances. With all their headquarters outside London, building societies employ around 52,300 full and part-time staff. In addition to digital services, they operate through approximately 1,300 branches, holding a 30% share of branches across the UK.

Executive Summary

We welcome this Phase 1 of the FCA's consultation, which we think successfully builds on DP1/23: Review of the Senior Managers and Certification Regime in assessing the extent to which the regime has met its objectives, as well as considering how it could be more effective and efficient.

Subject to our comments elsewhere in this response (most of which are matters of note/technical in nature rather than fundamental issues) we are supportive of the proposed Phase 1 changes which we agree will:

- Improve the efficiency of the 12-week rule,
- Streamline the Senior Management Function (SMF) approval process, including planning potential changes to processes and communications,
- Increase the validity period of criminal record checks for SMF applications
- Allow more time to report updates to Statements of Responsibilities (SoRs),
- Remove overlap in certification roles and provide guidance on annual certification to help firms streamline the process,
- Allow more time for firms to update specified Directory information, and
- Provide guidance in key areas.

We also look forward with anticipation to the FCA's planned Phase 2 work, as we believe that this has the potential to deliver an even more effective regime and drive more extensive efficiencies through considering:

- Reducing the number of SMF approvals, by removing SMF roles or reducing pre-approvals,
- Providing more flexibility to appoint interim SMFs before seeking approval by expanding the use of the 12-week rule,
- Further streamlining the SMF assessment process,
- Reducing further the frequency of submission of SoRs, the number of PRs, and simplifying Management Responsibilities Maps,

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- Designing a streamlined regime to replace certification,
- Removing the Directory and exploring with industry alternative ways to ensure consumers have other sources of information they require, and
- Streamlining Conduct Rule breach reporting, building on what is being done as part of Phase 1.

Questions in FCA CP25/21: Senior Managers & Certification Regime Review

Question 1: To what extent do you support the further changes we are considering in phase 2 of the reform (summarised in paragraph 1.11). Are there any other changes you suggest? We would welcome views on the impact (positive or negative) of each potential change and on any suggested additional improvements.

We are supportive, in so far as they have been summarised so far. Taking each of the areas currently referred to as forming part of Phase 2, we comment as follows on the scope for further change:

- **Reducing the number of SMF approvals, by removing SMF roles or reducing pre-approvals:** We have not focussed here on specific SMF roles that could be considered for removal. Instead, we would urge the FCA (and PRA) to consider applying a much more proportionate approach whereby small firms below an agreed size/asset threshold would have a much lighter touch applied, and a much reduced number of SMF roles.

- **Providing more flexibility to appoint interim SMFs before seeking approval by expanding the use of the 12-week rule:** We consider that the changes made as part of Phase 1will already help. However, allowing firms to appoint interim SMFs without the need for formal approval could ease the burden for both firms and the regulators.

- **Further streamlining the SMF assessment process:** There is undoubtedly scope to reduce/modify the number of documents that are requested and the systems used as part of the assessment process.

- **Reducing further the frequency of submission of SoRs, the number of PRs, and simplifying Management Responsibilities Maps:** All of these steps would in our view assist in streamlining and improving the processes around the SM&CR.

  In relation to SoRs, for example, options could include doing away with the requirement to submit a SoR, or extending the period even further on the basis that the firm itself maintains these (and an audit trail). This could then be audited as part of the firm's annual audit process, and/or considered as part of ongoing supervision work.

  There is also scope for the FCA to consider whether there are any current SMF roles (as well as Prescribed Responsibilities) that could be removed/covered by another existing SMF role.

- **Designing a streamlined regime to replace certification:** We do not consider that an entirely new regime should be introduced. As the FCA's own feedback to the DP demonstrates, the core aspects of the existing regime work well.

- **Removing the Directory and exploring with industry alternative ways to ensure consumers have other sources of information they require:** We consider that this will be trickier to achieve, given how the Directory has been designed to be used by firms and consumers alike. However, we look forward to reviewing any proposals that the FCA may have in relation to potential improvements or how the Directory's purposes could otherwise be achieved.

- **Streamlining Conduct Rule breach reporting:** Doing this through building on what is being done as part of Phase 1 seems a sensible approach.

Question 2a: Do you agree with our intention to improve forms, systems, communications and engagement with firms in relation to the application process?

The changes to Form A to allow reduction or consolidation of documentation will be welcome as will the ability for firms to include in a single document the evidence setting out the skills gap analysis, competency assessment and learning and development plan.

Question 2b: On which priority areas would firms welcome more information, guidance, or changes to forms?

Redesigning forms to improve clarity of language and accessibility and providing better guidance ought to improve the process for all parties. In addressing feedback in response to this question, we encourage the FCA to ensure that all areas of a particular form, system or process that would benefit from review/updating are addressed so far as possible at the same time.

Question 3: Do you agree to our proposals for changes to criminal record checks and disclosures?

We agree that changing the validity period for CRCs obtained for an SMF candidate from 3 to 6 months would provide clarity and more time for firms to use CRCs already obtained for an SMF candidate as part of the due diligence process in the SMF application.

We welcome the proposal to remove the requirement for firms to undertake CRCs where an existing SMF holder is applying for an SMF in the same firm or group.

We question the position that the FCA is taking on reportable misdemeanours as set out in paragraph 4.29. As the FCA points out in the immediately preceding paragraph it expects firms to determine whether a person is fit and proper. Surely the firm can be responsible for assessing that in the light of reportable misdemeanours? Adopting such an approach could further simplify and streamline the process.

Question 4: Do you agree with our proposed changes to the 12-week rule?

Firstly, we and many of our members recognise the issues with the current operation of the 12 week rule, as set out in paragraphs 4.33 to 4.35 of the CP.

Specifically, in relation to the proposals:

- **Time Period:** Changing the rule as proposed to effectively extend the period serves to address the issue around the time period being too short.

  However, we still believe that an extension of the 12 week period to 6 months in addition to the new proposal would be a more effective approach and would better sit with modern timescales for recruitment into senior roles. This in turn would be more likely to reduce the need for firms to apply for interim candidates, thus being less of a burden on both regulator and regulated.

  In the current drafting of the new Rule 10C.3A.8 R (2) it may be more helpful to refer to the application being "substantially" complete.

- **Guidance:** The practical examples set out in the table in the new Section 10C.3A.12 G are particularly helpful.

- **Conduct Rules:** It makes sense to apply these to the person performing an SMF role under the 12 week rule.

- **Prescribed Responsibilities:** We note that there is no proposal to change the current position whereby Prescribed Responsibilities should be reallocated to another SMF when the 12 week rule is in use.

  While we understand the rationale for this, we also believe that this may not be the most effective, efficient or least burdensome approach. Given the linkage between PRs and Responsibility Maps/Statements of Responsibility, an alternative approach could be to allow the person temporarily performing the role to hold the PR, thereby removing any consequential need to change the Statement of Responsibility that might otherwise arise. This would save time and effort for both firm and FCA.

  Further, such an approach appears to us to sit better with a situation where, as proposed, the person performing the Senior Management Function would not be specifically subject to the Senior Manager Conduct Rules.

Question 5: Do you agree with our proposals on SMF7?

The proposal to add guidance on when a person is captured by this function is welcome, subject to the detail of that guidance giving sufficient clarity on the point. We also note that the PRA is consulting on broadening the definition of SMF7 for dual regulated firms to include owners and controllers as appropriate, and that this will necessitate technical changes in the FCA Handbook.

Question 6: Do you agree with our proposals on SMF18?

Again, the proposed amended guidance in the draft Handbook text to emphasise considerations for firms in deciding if the SMF18 function applies will be helpful, subject to that amended guidance functioning as envisaged. Over time, and on the basis that the proposal will be implemented, it could be helpful for the FCA to monitor and report back on whether or not the stated aim of fewer SMF18 applications is realised.

Question 7: Do you agree with our proposals on Prescribed Responsibilities?

We agree that there is scope to explore the removal of some PRs, and additional guidance on splitting of PRs would be helpful and could be more useful for firms if supplemented by some practical examples.

It makes sense to amend the rule preventing SMF18 holding PRs to remove this restriction in relation to solo-regulated firms. However, it would make more practical sense to extend this to dual-regulated firms thereby removing the need for dual-regulated firms to obtain a waiver form both regulators should they seek to allocate a PR to SMF18. We would like to better understand the FCA's rationale for not taking this option to extend it, and encourage the FCA to comment more fully on that.

Guidance on allocation of FCA-designated PRs will be helpful. It is helpful that this will also cover PRs shared with the PRA where firms are dual-regulated, ad that there is no requirement/expectation that firms will reconsider their allocations in light of the guidance.

Question 8: Do you agree with our proposals on raising the thresholds for becoming an Enhanced SM&CR firm?

Yes, these are sensible and the proposal to introduce measures to ensure they remain in line with inflation are to be welcomed.

Question 9: Do you agree with our proposals on SoRs and MRMs?

Requiring updated SoRs (where there have been changes) to be submitted no later than 6 months after the last submission will be helpful in reducing firms' administrative burden. The proposed detailed Handbook provisions set out in the new SUP10C.11.6C G appear to us to be comprehensive and bring a good degree of clarity. However, on Sub-Clause (8), as referred to in our response to Question 10 below, a different approach may be better for all concerned.

We appreciate that the requirement to submit them at all is enshrined in the legislation but suggest that it is worth considering whether now is the time to change the legislative requirement, per our comments at Question 1. Would a more efficient and streamlined regime not be one where the SoR is maintained by the firm and only submitted to the regulator on request or as part of its supervisory work? If this is something that the FCA considers could be appropriate, we urge it to take steps to secure the legislative change needed to remove mandated submission and replace it instead with submission at the regulator's discretion, or similar.

Question 10: Do you agree with our proposal to align with the PRA on SoR submission requirements for dual-regulated firms?

In line with our comments in response to Question 7, we question the reason for a different approach being taken for dual-regulated firms, in this case the differing approach is stated as being linked to the need for the PRA to have a full audit trail. Why? Ought it not to be enough for the firm itself to have that, and in accordance with our comments elsewhere in this response, this sort of verification could of course be picked up during an audit process.

Question 11: Do you agree with our proposals on certification?

We note HMT's commitment to replace the current provisions of the Certification Regime in legislation and the intent that the FCA will work closely with them on developing a more proportionate regulatory approach in Phase 2.

We also note the FCA's contemplation of how to design a streamlined replacement regime if those legislative changes are made, and which would aim to ensure that non-SMF holders are fit and proper, while minimising the burden on firms.

Turning to the Phase 1 proposals:

- **Further Procedural Guidance:** In terms of the current proposals, the scope for firms to choose whether to adopt a more streamlined interim approach (pending the planned further reform) is welcome. Given the unnecessarily gold-plated approach adopted by some firms, issuing further guidance will be helpful. Clarification on the areas identified in the CP will also be helpful, namely:
    - No regulatory expectation/requirement to undertake annual criminal records checks.
    - The Certificate can be digital, but still in writing (as legislation requires).
    - Re-certification can be embedded in other processes such as performance reviews.
    - A proportionate approach to re-certification can be taken where there are no changes from the previous year.
- **Removal of Duplication:** We are supportive of the proposals to remove the need for separate certification (and hence inclusion on the Directory) where a person holds an additional certification function, as described in Sections 4.106 -4.108 of the CP. We also agree with the clarification that will be provided in guidance to make clear that there may be circumstances where a SMF may also need to be certified where the role is distinct and separate from their SMF role (eg a role such as advising on investments that needs a qualification).

We consider that the proposed Handbook wording at FIT2.1.3G (2) should be reassessed for clarity. As it stands it is unclear whether regards should be had to whether the person has simply been the "***subject of*** any…official investigation or public enquiry" or whether the person would need to have been "the ***subject of any***

adverse finding or settlement in … official investigation or public enquiry". This is due to the juxtaposition of "civil proceedings" in the clause.

Question 12: Do you agree with our proposal to change the timescales for updating the Directory?

We agree with the proposal to extend the time period for updating the Directory to 20 business days for most updates. However, a flat 4 week period may be more easily managed from a process perspective rather than having to calculate around Bank holidays, for example.

We note that the exception to this would be that details about staff leaving would still be required within the current 7 day period. We understand the rationale for this and agree with the proposal.

Question 13: Do you agree with our proposals on regulatory references?

Firstly, we and our members recognise some of the issues identified in the feedback received by the FCA – time taken by firms to respond to a reference request (with many taking the full 6 weeks); failure to respond; and the quality/value of information from non-financial services firms.

With that in mind, we are pleased to see the proposed reduction to 4 weeks of the time period within which regulatory references should be provided.

However, we would urge the regulators to go further than simply making this guidance, and to make it a rule. Without that, or some further parameters around/guidance on what would be considered more complex situations, we fear that many firms will simply retain the current practice of using the full period.

Question 14: Do you agree with the proposed guidance on the Conduct Rules?

We consider that it will be helpful to firms to have more guidance on application of the conduct rules. Similarly, we agree that focussing guidance on the following areas will be most useful:

- Making clear that only that only Conduct Rule breaches where specified disciplinary action (per FSMA S64C) was taken by the firm need to be notified to the regulator.

- Making clear that the notification requirements for breaches under SUP 15.11 are separate to any other reporting requirements.

- Outlining matters that the regulator might expect notification about pursuant to Senior Manager Conduct Rule 4.

- Clarifying the impact of legal privilege and Senior Manager Conduct Rule 4.

- Clarifying when cases in which the firm suspended an individual, or reduced or recovered their remuneration, need to be notified to the regulator.

- Clarifying regulatory reference expectations where an individual has breached a Conduct Rule and disciplinary action was not taken.

However, we have the following comments:

- In relation to notification of suspension, we agree in general that where the suspension is made before any investigation then that should not be reportable as a conduct rule breach. Our concern is that there may be extreme cases where the activity is certain/virtually certain to involve a conduct rule breach and in which firms may consider it more appropriate to report sooner rather than later. We would encourage the FCA to construct the guidance in such a way as to allow for that eventuality.

- We note that where there has been a reduction/removal of remuneration it will be made clear that firms should only report under SUP15.11 if the reason for the reduction or recovery was a sanction arising from a Conduct Rule breach. There may of course be circumstances where the reduction/removal was only in part for a Conduct Rule breach. The FCA should make clear that the reporting requirement covers reduction whether in whole or in part due to a Conduct Rule breach.

- It will be helpful to have clarity that a breach does not need to be included in a regulatory reference if:
    - The firm did not take disciplinary action as it did not consider the conduct to be serious enough to warrant it, and
    - The firm believes that the breach is insufficiently severe or serious to impact an assessment of fitness and propriety.

We encourage the FCA to provide sufficient clarity for firms/guidance on what types of breach might be "sufficiently sever or serious" to impact the F&P assessment.