Briefing

Financial Services Series
#8

May 2014

Significant Influence Functions and the Senior Managers regime

The current Significant Influence Functions ("SIF") regime will soon be replaced by a new Senior Managers regime for Banks. This month's briefing considers what SIFs are and key aspects of the approach towards them; what the new Senior Managers regime is and who it applies to; its enforcement; and its ramifications.

Since its inception, the FCA has shown a desire to "clean up" the image of the financial services industry. In particular it has placed a greater emphasis on the accountability of senior individuals in authorised firms.

Under the current Approved Persons regime, individuals wishing to perform a controlled function - most of which are SIFs - at an authorised UK firm need approval from either the FCA or PRA.

Bank staff will soon come under a new regime, derived from Part 4 of the Financial Services (Banking Reform) Act 2013 (the "Act"). The changes follow on from the Parliamentary Commission on Banking Standard's 2013 report on the deficiencies of the current system.

Significant Influence Functions

What are SIFs?

SIFs, as you might anticipate, are functions which the FCA has identified where the person responsible for their performance can exercise significant influence on the conduct of an authorised firm's affairs. As such, those holding SIFs are typically in senior roles.

The table below sets out the SIFs, which are split into categories of function.

Category of SIFs	Description of FCA-controlled function
FCA-governing functions	■ Director function ■ Non-executive director function ■ Chief executive function ■ Partner function ■ Director of unincorporated association function ■ Small friendly society function
FCA-required functions	■ Apportionment and oversight function ■ Compliance oversight function ■ CASS operational oversight function ■ Money laundering reporting function ■ Benchmark submission function ■ Benchmark administration function
Systems and controls function	■ Systems and controls function
Significant management function	■ Significant management function

The regulators have to approve candidates for SIF roles. Employers are expected to carry out due diligence on candidates, but the regulators will carry out their own investigations and routinely interview candidates for substantial roles such as chairman, chief executive, finance director and other important positions.

So, what is the current impact if you are deemed responsible for a SIF?

- "SIF Interview" by the FCA and/or PRA prior to approval;
- more intensive supervision by the FCA and/or PRA;
- possible disciplinary proceedings for breached regulatory requirements; and
- you may be asked to attest to the accuracy of information provided in response to FCA requests.

In practice, the SIFs system is currently linked to the Approved Persons regime. However changes are soon to be implemented for Banks under the Senior Managers Regime, putting the focus firmly on individual liability.

Senior Managers regime

Who will it apply to?

Under the Act, the new regime will apply to, broadly, Banks, Building Societies and Credit Unions (referred to in this briefing simply as "Banks"). At the moment only UK-incorporated Banks will be affected by the changes, although the Treasury may choose to extend the system to non-UK-incorporated Banks.

For the relevant institutions, the current regime will be replaced with:

(a) for junior employees, a licensing regime under which the Bank will be responsible for certifying that the employee is a fit and proper person to carry out his job; and

(b) a strengthened regime for the regulation of senior persons.

The regulators have not yet specified which roles will come under category (b), but it is likely to refer only to the most senior individuals in a Bank: those who carry responsibility for managing an aspect of the Bank's affairs that might involve a risk of serious consequences.

What will it mean for Senior Individuals in banks?

1. You will need to provide a "statement of responsibilities", setting out your key future responsibilities, whenever you apply for a senior management role;
2. Before relinquishing your role you will be required to prepare a "handover certificate" for your successor, clarifying key aspects of your role;
3. The Bank must notify the relevant regulator of any disciplinary action taken against a senior person;
4. The Bank must regularly check whether any grounds exist which might cause the regulators to withdraw their approval of a senior person;
5. Employers are required to carry out formal vetting of candidates for senior roles; and
6. The regulators will have the power to make approvals of senior persons subject to conditions or time limits.

How will it be enforced?

Significantly, the Act reverses the burden of proof; where there is a contravention by the firm and the senior person is responsible for the activities in relation to which the contravention occurred – it will be for the senior person to prove that they are not guilty of misconduct and that they took reasonable steps to avoid the contravention.

The Act also creates a new criminal offence of reckless misconduct leading to the insolvency of a Bank. The sanctions for this are high: an unlimited fine and/or up to seven years' imprisonment. However, we anticipate the regulators will mostly opt for disciplinary action as the elements of the criminal offence may prove difficult to establish.

Key Business impacts

These changes, and in particular the increased risk of disciplinary action, will add to the burden on senior managers. It may even discourage some individuals from taking up senior positions in Banks.

The new "statement of responsibilities" will be critical in light of the new reversed burden of proof. It will allocate key risks and activities to individuals who will be accountable for these matters. Care will need to be taken in drafting these and updating them to reflect any changes to the role and responsibilities.

It is likely that there will be important implications for a Bank's governance structure. For example, senior persons may become unwilling to delegate tasks which relate to their area of responsibility, and the consciousness of their potential exposure may make it harder to reach compromises and take collective decisions.

Conclusion

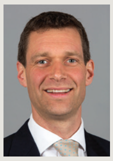
It is clear that the behaviour of senior individuals is coming under increasing scrutiny, with personal responsibility now being the focus. The FCA is being provided with increasing powers and tools with which to discipline those falling below the standards required.

Whilst senior individuals in Banks are currently the subject of the FCA's attentions, there have already been calls to apply the new regime, or something similar to it, across the financial sector. The impact of revised rules is likely to be felt more widely in the future.

Contacts

Kari McCormick, Tim Pope, and Hannah Miller advise clients on financial services disputes and regulatory matters, including enforcement. If you would like further information on the content of this article please contact them.

Kari McCormick
Partner
DDI: +44 (0)117 939 2259
Mobile: +44 (0)7917 284190
kari.mccormick@burges-salmon.com



Tim Pope
Legal Director
DDI: +44 (0)117 939 2230
Mobile: +44 (0)7968 225096
tim.pope@burges-salmon.com

Hannah Miller
Solicitor
DDI: +44 (0)117 939 2266
Mobile: +44 (0)7966 716599
hannah.miller@burges-salmon.com