

The Duty of Responsibility for insurers and FCA solo-regulated firms

Consultation Paper

CP17/42**

December 2017



How to respond

We are asking for comments on this Consultation Paper by 21 February 2018.

You can send them to us using the form on our website at: www.fca.org.uk/cp17-42-response-form.

Or in writing to:
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1 Summary

Why we are issuing this paper

- 1.1** This Consultation Paper (CP) relates to guidance on the 'Duty of Responsibility' to:
- insurance and reinsurance firms regulated by the FCA (which we call 'insurers' in the rest of this CP) and
 - firms regulated only by the FCA rather than also by the Prudential Regulation Authority (PRA) (which we call 'FCA solo-regulated firms' in the rest of this CP).

Who does this consultation affect?

- 1.2** The contents of this CP will be of interest to insurers, FCA solo-regulated firms and the senior management of both.
- 1.3** Consumers may also be interested in this CP, in particular how our approach sits within the FCA's broader priority to improve culture and governance in firms.

The wider context of this consultation

The introduction and extension of the Senior Managers and Certification Regime (SM&CR) and the Conduct Rules

- 1.4** Following recommendations by the Parliamentary Commission on Banking Standards, in its final report on professional standards and culture in the UK banking sector, Parliament passed the Financial Services (Banking Reform) Act 2013 (the Banking Reform Act). Amongst other changes, this introduced the Senior Managers Regime (SMR) and the Certification Regime.
- 1.5** These provisions came into force on 7 March 2016 for UK banks, building societies and credit unions, UK branches of non-UK firms with permission under the Financial Services and Markets Act 2000 (FSMA) to accept deposits and PRA-designated investment firms (collectively referred to in this CP as banking firms).
- 1.6** On the same date, we introduced, also under the Banking Reform Act, a new Code of Conduct, containing rules about the conduct of most employees of banking firms (Conduct Rules) and some staff of insurers. (See paragraph 1.13 for a summary of the Conduct Rules).
- 1.7** As a result of the Bank of England and Financial Services Act 2016 (the 2016 Act), the SM&CR will be extended to cover all insurers and FCA solo-regulated firms, from a date to be determined by the Treasury. In our consultation papers CP17/25¹ and

¹ CP17/25 *Individual accountability – extending the Senior Managers and Certification Regime to all FCA firms* (July 2017)



CP17/26², published in July 2017 (the July CPs) we set out how we propose to amend our Handbook, including the Conduct Rules, to reflect this extension.

The Senior Managers Regime

- 1.8** The SMR currently requires individuals (Senior Managers) to be pre-approved by the FCA or the PRA to perform Senior Management Functions (SMFs) on behalf of banking firms. The FCA and PRA designate these according to senior managers' roles and responsibilities.
- 1.9** When applying for the FCA's pre-approval for an individual to perform an SMF, a banking firm must submit a Statement of Responsibilities to us. This must set out the areas of the firm that the prospective Senior Manager will be responsible for managing. The firm must resubmit the Statement of Responsibilities whenever there is a significant change in the Senior Manager's responsibilities.
- 1.10** Certain types of banking firms must also prepare a management responsibilities map, setting out their governance and management arrangements, and how responsibilities are allocated to individuals, including Senior Managers, within the firm.
- 1.11** As part of the extension of the SM&CR, we have proposed that FCA solo-regulated firms will also have to prepare Statements of Responsibilities and that some will also have to prepare management responsibilities maps. Insurers are already under similar obligations. We have proposed that those obligations will change slightly, for some insurers, on the extension. The details of these proposed changes are set out in the July CPs.
- 1.12** When taking disciplinary action against a Senior Manager – whether under the Conduct Rules, the Duty of Responsibility (see Chapter 2) or otherwise – we will consider the Senior Manager's Statement of Responsibilities and, if applicable, the relevant firm's management responsibilities map when determining the extent of the Senior Manager's responsibilities in the firm at the time of the contravention.

The Conduct Rules

- 1.13** The Conduct Rules set basic standards of good conduct for most staff of banking firms and some staff of insurers. In the July CPs we proposed that when the SM&CR is extended, the Conduct Rules will additionally apply to staff of insurers and FCA solo-regulated firms who carry out financial services work. We may take disciplinary action against individuals whose conduct falls short of these standards.
- 1.14** There are particular Conduct Rules that apply only to Senior Managers. These Conduct Rules include requirements that firms take reasonable steps to ensure that the business of the firm is controlled effectively, that the business complies with regulatory requirements and that any delegation of responsibilities is appropriate and properly overseen.

The Duty of Responsibility

- 1.15** The Duty of Responsibility was introduced in the 2016 Act and came into force on 10 May 2016. It currently applies to Senior Managers of banking firms and as explained in the July CPs, it will also apply to Senior Managers of insurers and FCA solo-regulated firms when the SM&CR is extended.

² CP17/26 *Individual accountability – extending the Senior Managers and Certification Regime to insurers* (July 2017)

2 The Duty of Responsibility

- 2.1** The Duty of Responsibility specifies that we can take action against a Senior Manager where:
- there was a contravention of a relevant requirement by the Senior Manager's firm
 - at the time of the contravention or during any part of it, the Senior Manager was responsible for the management of any of the firm's activities in relation to which the contravention occurred, and
 - the Senior Manager did not take such steps as a person in their position could reasonably have been expected to take to avoid the contravention occurring or continuing
- 2.2** When enforcing the Duty of Responsibility, the burden of proof lies on the FCA to show that the Senior Manager did not take the steps a person in their position could reasonably have been expected to take to avoid the firm's breach occurring or continuing.
- 2.3** Our Decision Procedure and Penalties Manual (DEPP), in our public Handbook, already sets out (in DEPP 6.2.9-A G to 6.2.9-F G) guidance as to:
- the circumstances in which we will apply the duty
 - a non-exhaustive list of considerations that may be relevant when determining whether a Senior Manager was responsible for the management of any of a firm's activities in relation to which a contravention of a relevant requirement by the firm occurred, and
 - a non-exhaustive list of considerations we will keep in mind when determining whether a Senior Manager took the steps such a person in their position could reasonably have been expected to take to avoid the firm's contravention occurring or continuing
- 2.4** Definitional changes to our Handbook already proposed in the July CPs, will have the effect of applying the guidance in DEPP 6.2, to Senior Managers of insurers and FCA solo-regulated firms. We do not believe we need to amend that guidance to reflect the extension of the duty to such Senior Managers. We summarise in the paragraphs immediately below, some of the important factors we took into account when producing the guidance in DEPP 6.2. The guidance is not prescriptive about the steps that a Senior Manager should take to avoid a firm contravention occurring or continuing, as the steps reasonably expected, will vary from case to case depending on the circumstances. Nor, for this reason, does it set out examples of the steps reasonably expected of Senior Managers at specific types of firms.
- 2.5** When we are considering whether a Senior Manager has complied with the duty, we will look at whether the Senior Manager acted in accordance with their statutory, common law and other legal obligations, including, but not limited to, the Conduct Rules (and



other relevant rules) set out in our Handbook. There is considerable guidance on the reasonable steps a Senior Manager must take in the Conduct Rules.

- 2.6** In producing the existing guidance in DEPP, we addressed the relevant responses to our consultations on guidance we proposed for the presumption of responsibility³, which the Duty of Responsibility replaced. We summarise our position on those responses by subject matter below.

The effect of findings against a firm on a separate action brought by the FCA against a Senior Manager under the Duty of Responsibility – DEPP 6.2.9-A G

- 2.7** Our existing guidance, at DEPP 6.2.9-A G, states that, in an action brought by the FCA against a Senior Manager under the Duty of Responsibility, the Senior Manager is not bound by a finding of the FCA's Regulatory Decisions Committee, a court or a tribunal to which they were not privy nor party.

The threshold for enforcement action under the Duty of Responsibility

- 2.8** We will decide whether to take action based on the Duty of Responsibility by applying our published criteria in DEPP. We will look at all the circumstances of the case, including the seriousness of the breach, the relevant individual's position, responsibilities and seniority and the need to use enforcement powers effectively and proportionately. We do not believe that there is a need for any additional threshold.

Whether the FCA will apply standards retrospectively – DEPP 6.2.9-D G

- 2.9** We will not apply standards retrospectively or with the benefit of hindsight. This is reflected in our guidance at DEPP 6.2.9-D G. Our guidance states that, when we apply the Duty of Responsibility, we will consider what steps a competent Senior Manager would have taken at that time, in that specific individual's position, with that individual's role and responsibilities in all the circumstances.

The extent of a Senior Manager's responsibilities – DEPP 6.2.9-C G

- 2.10** We have not stated in our guidance that the Duty of Responsibility will only apply in relation to a Senior Manager's responsibilities set out in their Statement of Responsibilities. This is because it is possible for Senior Managers to be responsible for the management of activities at their firm that fall outside their prescribed responsibilities and such guidance could fetter our ability to rely on the duty in a way not specified by Parliament.

- 2.11** Whether a Senior Manager was responsible for the management of any of a firm's activities will be a question of fact. We may not be able to check that any Statements of Responsibilities and management responsibilities maps fully and accurately describe the activities a Senior Manager was responsible for managing without looking behind them. So Statements of Responsibilities and management responsibilities maps will be relevant considerations, but there will be additional relevant considerations.

The relevance of the considerations regarding reasonable steps to all Senior Managers – DEPP 6.2.9-E G

- 2.12** All the considerations in DEPP 6.2.9-E G are potentially relevant to an assessment of the steps reasonably expected of all Senior Managers, whatever their role and responsibilities.

³ FCA CP14/13 and PRA CP14/14 *Strengthening accountability in banking: a new regulatory framework for individuals* (July 2014); and CP15/9 *Strengthening accountability in banking: a new regulatory framework for individuals* (March 2015)

2.13 For this reason, we do not distinguish in our guidance between considerations that may only be relevant to Senior Managers performing an executive role, and considerations that may only be relevant to Senior Managers who are non-executive directors. What is reasonable in relation to each consideration will depend on the specific individual's position, role and responsibilities and all the circumstances.

2.14 Our guidance does, however, make allowance for the fact that the steps a Senior Manager in a non-executive role could reasonably have been expected to take may differ, depending on the circumstances, from those reasonably expected of a Senior Manager in an executive role.

Collective decision-making – DEPP 6.2.9-E G (15)

2.15 Under the Duty of Responsibility, Senior Managers are accountable for their individual contributions to collective decisions and their implementation insofar as they concern any of the firm's activities for which they are responsible.

Competing priorities

2.16 We decided that we would not state in our guidance that we would expect to have regard to whether a Senior Manager took reasonable steps to manage competing priorities, when determining whether a Senior Manager took such steps as a person in their position could reasonably have been expected to take to avoid the firm's contravention occurring or continuing.

2.17 We did not believe that would be helpful, as it does not clarify the steps reasonably expected of Senior Managers when doing so. We also wanted to avoid giving the impression that Senior Managers will not be guilty of misconduct under the Duty of Responsibility merely by demonstrating that they were faced with competing priorities, or that it is acceptable for a busy Senior Manager to deprioritise concerns about conduct.

2.18 Our guidance states that, when determining whether a Senior Manager took such steps as a person in their position could reasonably have been expected to take to avoid the firm's contravention, we must consider all the circumstances. It also states that we would expect to have regard to whether a Senior Manager delegated appropriately, and to the nature, scale and complexity of the firm's business.

The PRA

2.19 We worked closely with the PRA to ensure that our guidance on the Duty of Responsibility is consistent and aligned with its guidance.

What do you need to do next?

2.20 We want to know what you think. Please send us your comments by 21 February 2018 by using the online form on our website, email us at cp17-42@fca.org.uk or write to us at the address on page 2.



What will we do next?

- 2.21** We will consider your feedback and publish a Policy Statement in 2018, setting out whether any further changes to our Handbook, beyond those proposed in the July CPs, need to be made to reflect the extension of the Duty of Responsibility to insurers and FCA solo-regulated firms.
- 2.22** As indicated above, the extension of the Duty of Responsibility is subject to agreement by the Treasury. We have assumed that the extension of the SM&CR to insurers will commence in late 2018, followed by commencement of the regime for FCA solo-regulated firms in mid to late 2019. We anticipate that the extension of the Duty of Responsibility will align with these start dates. The actual commencement date will be announced and set by the Treasury in due course.

3 Extension of our relevant Handbook guidance

- 3.1** As noted above, this CP follows the July CPs which set out our approach to the extension of the SM&CR to insurers and FCA solo-regulated firms. It also follows CP16/26⁴, in which we consulted on guidance as to how we would enforce the Duty of Responsibility on Senior Managers of banking firms, and our Policy Statement 17/9⁵, which set out our corresponding policy and final guidance.

Related FCA Publications

CP17/25 – Extending the SM&CR to all FCA firms

CP17/26 – Extending the SM&CR to insurers

PS17/9 – Guidance on the duty of responsibility: final amendments (including feedback on CP16/26) to DEPP

CP16/26 – Guidance on the duty of responsibility: amendments to DEPP

Related PRA Publications

CP14/17 – Strengthening individual accountability in insurance: extension of SM&CR to insurers

Supervisory Statement 28/15 – Strengthening individual accountability in banking

- 3.2** Definitional changes to our Handbook already proposed in the July CPs, will have the effect of applying the guidance in DEPP 6.2, to Senior Managers of insurers and FCA solo-regulated firms. We have considered whether that requires us to amend guidance to reflect the extension of the duty to such Senior Managers. We do not believe it does.

Q1: **Do you agree that no changes need to be made to our Handbook, beyond those already proposed in our July CPs, to reflect the extension of the Duty of Responsibility to Senior Managers of insurers and FCA solo-regulated firms?**

If not, what changes do you believe should be made and why?

⁴ CP16/26 *Guidance on the duty of responsibility: amendments to the Decision Procedure and Penalties Manual* (September 2016)
⁵ PS17/9 *Guidance on the duty of responsibility: final amendments (including feedback on CP16/26) to the Decision Procedure and Penalties Manual* (May 2017)



Annex 1

Question in this paper

Q1: Do you agree that no changes need to be made to our Handbook, beyond those already proposed in our July CPs, to reflect the extension of the Duty of Responsibility to Senior Managers of insurers and FCA solo-regulated firms?

If not, what changes do you believe should be made and why?

Annex 2

Cost benefit analysis and equality and diversity

Cost benefit analysis

1. The Duty of Responsibility is part of the SMR, an element of the SM&CR. The costs incurred by firms to familiarise themselves with our guidance and act on it and the benefits arising from that are covered by the cost benefit analysis for our SM&CR policy proposals.⁶ Further, this CP does not impose any material additional costs on firms beyond those costs intended by the legislation under which the Duty of Responsibility was introduced and is to be extended. Therefore we have not conducted a cost benefit analysis for this proposal.

Equality and diversity

2. We are required under the Equality Act 2010 to 'have due regard' to the need to eliminate discrimination and to promote equality of opportunity in carrying out our policies, services and functions.
3. We have considered whether there are any potential equality or diversity impacts of this CP. We do not think there are any, but we would welcome your comments.



Annex 3

Abbreviations used in this paper

Banking firms	UK banks, building societies and credit unions, UK branches of non-UK firms with permission under FSMA to accept deposits and PRA-designated investment firms
Banking Reform Act	Financial Services (Banking Reform) Act 2013
Conduct Rules	Code of Conduct in the FCA's Handbook
CP	Consultation Paper
DEPP	The Decision Procedure and Penalties Manual in the FCA's Handbook
FCA	Financial Conduct Authority
FCA solo-regulated firm	A firm regulated only by the FCA rather than also by the PRA
FSMA	The Financial Services and Markets Act 2000
Handbook	The FCA's Handbook of rules and guidance
Insurer	An insurance or reinsurance firm regulated by the FCA
July CPs	FCA CPs 17/25 and 17/26, published in July 2017
PRA	Prudential Regulation Authority
Senior Manager	A person approved to perform a Senior Management Function
SMF	Senior Management Function
SMR	Senior Managers Regime
SM&CR	Senior Managers and Certification Regime
2016 Act	Bank of England and Financial Services Act 2016

Disclaimer

We have drafted this CP in the context of the existing UK and EU regulatory framework. The Government has made clear that it will continue to implement and apply EU law until the UK has left the EU. We will keep the CP under review to assess whether any amendments may be required in the event of changes in the UK regulatory framework in the future.

We make all responses to formal consultation available for public inspection unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.

Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

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