Financial Conduct Authority

# Regulator Assessment: Qualifying Regulatory Provisions

**Title of proposal:** Accountability regime for banking sector (Policy statement in CP15/22; consultation and cost-benefit analysis in CP14/13)

**Lead regulator:** FCA

**Date of assessment:** 29 July 2016

**Commencement date:** 7 March 2016

**Origin:** Domestic

**Does this include implementation of a Cutting Red Tape review?** No

**Which areas of the UK will be affected?** UK Banks, building societies, credit union, and dual-regulated investment firms

UK branches of overseas banks

## Brief outline of proposed new or amended regulatory activity

Following the 2008-09 financial crisis, in June 2012 Parliament established the Parliamentary Commission on Banking Standards (PCBS) to consider and report on professional standards and culture of the UK banking sector, and lessons to be learned about corporate governance, transparency and conflicts of interest, and their implications for regulation and for Government policy.

The PCBS concluded that public trust in banking was at an all-time low and recommended a series of measures to restore trust and improve culture. These recommendations proposed a new framework for approving and holding individuals to account which would include:

- a Senior Persons Regime to replace the Significant Influence Function (SIF) element of the Approved Persons Regime for deposit-takers and PRA designated-investment firms with a Senior Management Function, covering a narrower range of individuals
- a Licensing Regime (which subsequently became the Certification Regime under the Banking Reform Act) operating alongside the Senior Persons Regime and applying to other bank staff whose actions or behaviour could significantly harm the bank, its reputation or its customers, and

- replacing the existing Statements of Principle and Code of Conduct for Approved Persons with a set of enforceable Conduct Rules which would apply to a wider range of employees than those subject to regulatory approval.

The changes made by the Accountability Regime reflect the recommendations of the (PCBS) and implement changes required by amendments which the Financial Services (Banking Reform) Act 2013 (the Act) made to the Financial Services and Markets Act 2000 (FSMA). These changes were significant and include:

- A new 'Senior Managers Regime' (SMR) for individuals who are subject to regulatory approval, which requires firms to allocate a range of responsibilities to these individuals and to regularly vet their fitness and propriety. This focuses accountability on a narrower number of senior individuals in a firm than the previous Approved Persons Regime (APR).

- A 'Certification Regime' which requires relevant firms to assess the fitness and propriety of certain employees who could pose a risk of significant harm to the firm or any of its customers.

- A new set of 'Conduct Rules'.

The new Regime creates a framework to encourage individuals to take greater responsibility for their actions, and will make it easier for both firms and regulators to hold individuals to account.

## Which type of business will be affected? How many are estimated to be affected?

Our new rules apply to UK banks, building societies, credit union, and dual-regulated investment firms. There are 160 banks and investment firms, 45 building societies and 523 credit unions.

| **Price base year** | **Implementation date** | **Duration of policy (years)** | **Business Net Present Value** | **Net cost to business (EANDCB)** | **BIT score** |
|---|---|---|---|---|---|
| 2014 | 2016 | 10 | -£490.9m | £55.1m | £275.5m |

## Please set out the impact to business clearly with a breakdown of costs and benefits

We have assessed three types of impacts on affected businesses:

- Compliance costs (one off) – estimated at £260.62 million

- Compliance costs (ongoing) – estimated at £26.75 million per annum

- Indirect and wider impact

| | **One off Costs** | **Ongoing costs, per annum** |
|---|---|---|
| Banks | £236.6m | £22.6m |
| Building societies | £19.25m | £2.91m |
| Credit Unions | £4.77m | £1.24m |
| **Sector Total** | £260.62m | £26.75m |

**Compliance costs**

Compliance cost cover both one-off and ongoing costs, defined as follows:

- One-off costs are those incurred once off in complying with the policy. Examples include developing guidance; setting up IT systems; or providing training on the migration.

- Ongoing costs are those incurred annually as a result of the policies, for example ongoing training obligations; or annual reviews of responsibilities.

Below we present the key cost drivers for both ongoing and one-off costs associated with the individual policy proposals. In each case, to construct the monetary value of the cost estimate we have multiplied the expected time involved in complying with the average remuneration of the individuals that would be involved (including overheads). Where the cost is for a new system or infrastructure, or relates to outsourced activities, we have used the estimated cost of purchasing such inputs. For a more detailed breakdown of compliance costs, see Annex 10: *Cost Benefit Analysis of the New Regime for Individual Accountability and Remuneration*, Consultation Paper 14/13, FCA.

<u>Migration to Senior Management Function Regime</u>

The one-off costs to firms of migrating to the SMF regime may be incurred either internally and/or through

third party costs (e.g. legal advice) and include:

- Understanding the regulation.

- Deciding, and developing guidance on, the definition of the SMF and who would be captured.

- Guidance for persons who will become SMF's to ensure they understand their duties and responsibilities under the new regime.

- Revision of the organisational structure of the firm.

<u>Criminal offence and presumption of senior management responsibility</u>

The costs associated with complying with this element of the SMF regime cover the costs of recording and retaining additional evidence to support the presumption of senior management responsibility (i.e. in the event than an individual in an SMF role is required to demonstrate proof that he/she took all reasonable steps to avoid a regulatory breach). We do not consider there to be any direct compliance costs of the new criminal offence.

The one-off costs here could include:

- Setting up systems to record additional information.

- Legal advice associated with recording and retaining evidence.

Ongoing costs could include:

- Annual costs of recording and storing additional information.

<u>Statement of responsibility (SoR)</u>

The one-off costs associated with this policy include:

- Developing an SoR for each individual in a SMF role.
- Developing a 'responsibilities matrix' including all important functions set out by the FCA.
- Developing guidance relating to handover certificates.

The days required would both be per SMF individual (i.e. training) or in aggregate (e.g. a project team).

In addition, ongoing costs would include:

- Maintaining the responsibilities matrix. This would be either a general annual review or a revision each time an individual left a role, in which case it is linked to the turnover of SMFs individuals.
- Developing and retaining handover certificates.

Pre-approval

The one-off costs associated with this policy would include updating any policies or processes to provide additional information as part of the SMF pre-approval application. The ongoing costs would include additional time required for firms to submit an application for SMF pre-approval given the need for additional information.

Migration to the Certified Persons regime

The one-off costs associated with migrating individuals to the CP regime might include:

- Developing guidance/documentation on who is a CP.
- Changes to organisational structure.
- Migrating people/ functions to the new regime.

There may be some on-going costs associated with updating documentation if the CP population changes although these are likely to be limited.

Continuing fit and proper

If firms require a new system to ensure continual 'fitness and propriety checks', possibly through amendments to current appraisal processes this would represent a one-off cost.

Ongoing costs could include undertaking additional checks (e.g. request declarations from staff that there has been no change to their fitness and propriety).

These policies also propose DBS8 checks for senior managers (either on an annual or periodic basis), which would impose ongoing costs of an update check (we assume that DBS checks are already conducted for senior managers upon hiring and therefore this implies no one-off costs).

Requesting regulatory references that go back five years could have one-off costs of setting up processes top request and provide this information, and ongoing costs of additional time spent in requesting and (more relevant) providing the information.

Rules of conduct

The costs of this policy will depend on the population included within the scope of 'relevant persons' and the extent to which firms already have a Code in place across some/all employees.

The one-off costs associated with this policy include:

- Developing or updating documentation/ guidance on conduct rules.
- Developing or updating any ongoing training material.
- Switching current staff over to new rules (both staff currently familiar with an existing code, and staff who are not currently subject to any code).

The ongoing costs would include:

- Where a firm does not currently have any Code in practice, time required to train staff in the new

Code upon hiring. This cost would be related to staff turnover.

- Where a firm does not currently have any Code in place, annual revision training for all affected staff.
- Where a firm does currently have a Code in place, any additional time implied by adopting the new Code.

Notifying breaches of misconduct

The costs of this policy will also depend on the scope of 'relevant persons' and the extent to which firms already monitor and report conduct breaches. The one-off costs could include:

- Setting up / amending systems to record and report conduct breaches. This would include internal resources and external or IT costs.

Ongoing costs could include:

- New or additional reporting processes.

## Please provide any additional information (if required) that may assist the RPC to validate the BIT Score.

The changes made by the Accountability Regime reflect the recommendations of the Parliamentary Commission on Banking Standards and implement changes required by the amendments which the Financial Services (Banking Reform) Act 2013 made to the Financial Services and Markets Act 2000 (FSMA).

Given the significance of these changes and the one-off and on-going compliance costs to firms, we believe that had this policy initiative taken place in the future it would be reasonable for the FCA to split the costs of implementation with HMT. As a retrospective measure we have not attempted to split the costs in this instance.