Association of Mortgage Intermediaries' response to FCA CP17/25
Individual Accountability: Extending the Senior Managers & Certification Regime (SMCR) to all FCA firms

This response is submitted on behalf of the Association of Mortgage Intermediaries (AMI). AMI is the trade association representing over 80% of UK mortgage intermediaries.

Background

Intermediaries active in this market act on behalf of the consumer in selecting an appropriate lender and product to meet the individual consumer's mortgage requirements. Our members also provide access to associated protection products.

Our members are authorised and regulated by the Financial Conduct Authority (FCA) to carry out mortgage and insurance mediation activities. Firms range from sole traders through to national firms and networks, with thousands of advisers.

We welcome the opportunity to respond to these proposed changes which have the potential to significantly impact our member firms and their customers. The extended timetables for implementation are both required and supported.

Response

Inclusion of appointed representatives

As we stated under the work on the Mortgage Market Review, developing solutions in piecemeal is less than satisfactory as it is usually only with the entire picture that we can ensure the solutions are workable and effective. The decision to defer the work on the application of the regime to appointed representative firms and their staff is an issue for us as we are unable to comment on a complete picture.

Accordingly, we are deeply concerned that the FCA has proposed to exclude appointed representatives from the Senior Managers & Certification Regime (SMCR), which has the potential to create an un-level playing field across firms. Applying a different regulatory regime to the network business model will create unfair commercial advantages/disadvantages, leading to a potential competition issue. We do not agree that the FCA is restricted by legislation, and believe that the FCA has scope to extend SMCR to all firms.

FSMA defines "employee" in Section 63 E (Certification of employees by relevant authorised persons). Section 63 E (9) (which is currently referred to in the FCA handbook glossary as the relevant definition for SYSC 5.2 and is proposed to be referred to in the new SYSC 27) says:

"(9) *In this section any reference to an employee of a person ("A") includes a reference to a person who—*

(a) *personally provides, or is under an obligation personally to provide, services to A under an arrangement made between A and the person providing the services or another person, and*
(b) *is subject to (or to the right of) supervision, direction or control by A as to the manner in which those services are provided*"

"Employee" is commonly understood to mean an individual. Under section 230(1) of the Employment Rights Act 1996, an employee is defined as: "*an individual who has entered into or works under (or, where the employment has ceased, worked under) a contract of employment*". Under section 230(2) of the Employment Rights Act 1996 a contract of employment means: "*a contract of service or apprenticeship, whether express or implied, and (if it is express) whether oral or in writing*".

We are not suggesting that the definition of employee encompasses appointed representatives (ARs), which would not be consistent with their tax treatment, or our desired outcome. Nevertheless we consider that the FCA have under FSMA the scope to extend the certification regime to the full scope of the definition by reference to the use of the term "*person*" (which includes companies and other corporate bodies) rather than only to individuals. Also, the FSMA definition (unlike the Employment Rights Act 1996) is not limited to contracts of service so contracts for services are also within scope.

A person who works for an AR of a relevant firm may therefore be covered by the certification regime if they fall within the description of employee given above. It will be a question of fact in each case whether the person "*personally provides, or is under an obligation personally to provide, services"*.

The term "*personally provides*" was used in other legislation, notably the IR35 legislation on the taxation of individuals providing services through a company or other intermediary, where the person must be subject to a certain degree of direction, supervision or control by the engager (as might be the case under an AR agreement) and factors such as an entitlement to provide a substitute to do the work points away from services being personally provided. We are grateful that the FCA is taking time to ensure this is implemented correctly as network principals do not see themselves as employers of their ARs as they would not usually dictate the place, time or intensity of work.

In addition we consider that some firms which have both directly authorised (employed) staff and ARs will have little option but to bring all senior management and advisers into SMCR, whilst other networks who only have ARs might adopt a less stringent interpretation of the requirements. Any creation of a two-tier structure must be avoided by the FCA.

FCA register

The FCA's obligation to maintain the register in respect of ARs are primarily in sections 39 and 347 of FSMA. We therefore believe that the FCA must continue to maintain a register of all mortgage ARs.

Removing ARs from the FCA register would be in contravention of European legislation. Article 29 (4) and Article 31 (4) (specifically referring to appointed representatives, and referring to Article 29 (4) for the minimum information on the register) of the Mortgage Credit Directive (MCD) set out the explicit requirement for ARs to be included on a public register.

In implementing MCD, the Mortgage Credit Directive Order 2015 in Schedule 1 amended FSMA s39 and also amended FSMA s347 (1) to include a new obligation on the FCA to include in the register "*in the case of an appointed representative to whom subsection (2B) applies, the name of the mortgage intermediary on whose behalf the appointed representative acts*"; S347 (2B) applies to "*an appointed representative to whom section 39(1BA) applies or to whom that subsection would apply if the requirements of section 39(1BB).*"

FSMA section 39(1BA) sets out that:

"(*1BA)* *This subsection applies to a person (“A”)—*

(a) *if A's principal is a mortgage intermediary, and*

(b) *so far as the business for which A's principal has accepted responsibility is of a kind—*

  i. *specified in article 25A (arranging regulated mortgage contracts), article 36A (credit broking), article 53A (advising on regulated mortgage contracts) or article 53DA (advising on regulated credit agreements the purpose of which is to acquire land) of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001; and*

  ii. *to which the mortgages directive applies,*

unless A meets the requirements of subsection (1BB).

(1BB) *The requirements of this subsection are—*

(a) *that A is entered on the record maintained by the FCA by virtue of section 347(1)(hb);*

(b) *that A's principal is a person who has a Part 4A permission to carry on one or more of the regulated activities mentioned in subsection (1BA)(b)(i); and*

(c) *that A's principal is not a tied mortgage intermediary."*

In addition, we cannot see how excluding ARs from the FCA register would sit within the FCA's consumer protection objective under FSMA section 1C, and the FCA's general duties under FSMA Section 1B of taking action to minimise the extent to which it is possible for a person to carry on business in contravention of the general prohibition (the ability to check ARs on the register being a material part of that).

Questions

Q1. Does the proposed list of Senior Managers in the core regime cover the appropriate roles, i.e. the most senior decision makers within a firm?

We would like clarification on the compulsory Senior Management Functions (SMFs) that firms must apply. The FCA has provided assurances that firms will only have to apply SMFs where there are individuals performing these jobs already, rather than needing to restructure their business. However the description “required functions” has led some to believe that all core firms must apply all 3 of these SMFs. We would welcome clarification from the FCA on this, as we believe mortgage intermediary firms would not be required to allocate SMF16 under the proposed rules (SUP 10C.6.1). This is consistent with the current approach where our firms are not required to apply CF10.

However we are still in discussion with the FCA policy team on the applicability of certain aspects of the debt management function within the consumer credit regime. We continue to await confirmation that mortgage firms are not required to apply CF10 under CONC as they are not carrying out debt management activity. With the SMCR proposals building on these requirements, we repeat our request for explicit confirmation that our firms will not fall under the requirements to apply SMF16. Until this is clarified responding full to this question remains difficult.

We would also like clarification on the FCA’s expectations of firms who have different structures to those assumed in the proposals, such as those whose chairs of committees are executives rather than non-executive directors, and those who outsource certain functions.

Q2. Are there any other roles that the FCA should consider specifying as SMFs? (You may wish to consider the list of proposed Senior Managers under the enhanced regime in section 8.16)?

We consider these as appropriate for mortgage and protection firms.

Q3. Are there any proposed Senior Managers that the FCA should consider excluding from the core regime?

We consider these as appropriate for mortgage and protection firms.

Q4. Do you agree with our approach to Senior Management Functions for Limited Scope Firms? If not, please explain why.

We believe the proposed definition of Limited Scope Firms is too narrow. There is not enough proportionality to ensure that small firms are not burdened with unnecessary layers of bureaucracy and inappropriate structures. We believe the FCA should consider extending the Limited Scope regime to firms with a sole proprietor and up to 4 employees. These firms are likely to only have one person who will be allocated the SMFs (the proprietor) in any case. In that case the proprietor should be able to certify that they have control, undertake all regulatory functions and accept liability in the same way as a sole trader.

Q5. Do you agree with our proposed list of Prescribed Responsibilities? If not, please explain why.

We consider these as appropriate for mortgage and protection firms.

Q6. Do you agree with our proposed Prescribed Responsibility for AFMs as set out in CP17/18? If not, please explain why.

This is not our area of expertise.

Q7. Do you agree with the functions we have proposed making Certification Functions? If not, please explain why.

Yes.

Q8. Are there any other functions that we should make a Certification Function?

No.

Q9. Do you think the identity of people performing Certification Functions should be made public by firms? If so, which Certification Functions should be made public?

We believe that the Certification Functions should be made public on the FCA register as a central source, rather than maintained by individual firms. This would ensure the FCA continues to meet its consumer protection objective. We would not want to see the undoing of the good regulatory work that has been carried out to help protect consumers from scams nor the regulator absolve this crucial responsibility.

This would mean those currently holding CF functions would continue to appear on the register, but also the extension of some functions not currently listed, such as mortgage advisers. This was proposed and agreed under the Mortgage Market Review and we still consider it to be an essential development which had and still has our full support. In the interests of transparency with customers and in maintaining their confidence in financial services firms, we support the inclusion of all those holding proposed Certification Functions to be made available on the FCA register. As the FCA defines these individuals' jobs as having "a big impact on customers, the firm and/or market integrity", we cannot see how any of these roles could not be made public.

Given that firms already submit returns, under SMCR firms would simply continue to notify the FCA of their staff with Certification Functions.

Q10. Do you agree with our proposed territorial limitation for the Certification Regime? If not, please explain why.

No comment.

Q11. Do you agree with the approach we have proposed to allocating CASS responsibilities? If not, please explain why.

No comment.

Q12. Do you agree with our proposed approach to rules and guidance on the fit and proper test? If not, please explain why.

We are generally supportive of the proposals. However, it is not clear how the Fit and Proper requirements apply to Limited Scope firms in practice. Although the proposed rules on conducting criminal checks would not apply to a sole trader as the only Senior Manager, the proposed rules seem to suggest that the sole trader is supposed to annually assess their own fitness and propriety, carry out credit checks on themselves, and write their own regulatory references. We would consider that as the FCA will conduct the initial fitness and propriety assessment, then they should conduct an annual assessment. Alternatively the FCA should require the principal of the Limited Scope firm to annually certify to the FCA that they have not committed any criminal offences, have kept up to date on industry developments and do not have personal financial issues.

Q13. Do you agree with our proposed requirements on criminal record checks? If not, please explain why.

Yes.

Q14. Do you agree with our proposed requirement of regulatory references? If not, please explain why.

Clearer guidance on regulatory references is required. The proposed rules do not require firms to disclose information that has not been properly verified, including if an ex-employee left during disciplinary proceedings. The FCA however proposes that a firm may include such information “if it wishes to” (SYSC 22.5). We would like the FCA to set clearer boundaries.

The requirement for firms to disclose to a prospective employer any serious misconduct, breaches of the Conduct Rules and whether the employee breached the fit and proper test (no matter how the individual’s employment ended) means that compromise agreements are unlikely to be possible going forward. In particular, the proposed rules set out that “a firm should not give any undertakings to suppress or omit relevant information in order to secure a negotiated release” (SYSC 22.5.15). We believe the FCA should be communicating the prohibition of compromise agreements as part of the consultation/implementation narrative.

Q15. Do you agree with our proposal to apply the Conduct Rules to financial services activities?

Yes.

Q16: Do you agree with our proposal to apply the Conduct Rules to all employees who perform financial services, with the limited exclusions listed in section 7.14?

Yes.

Q17. If you disagree, please explain why, including (where appropriate) cost implications?

N/A.

Q18. Do you agree with our proposal to link notification requirements for disciplinary action to breaches of the Conduct Rules?

Yes.

Q19. Do you agree with our proposed frequency of Conduct Rules notifications? If not, please explain why?

Yes.

Q20. Do you agree with our proposed approach of using the objective criteria set out above to identify firms for the enhanced regime? If not, please explain why and propose alternative approaches.

We understand the simple approach taken to apply a single turnover number which will give clarity on when firms would move to the enhanced category. However we believe that the FCA should consider taking a risk management approach to defining enhanced firms, i.e. firms holding client assets could cause greater harm to consumers than an intermediary, who does not hold client money, with a large revenue. Under such an approach a pure intermediary firm might have a threshold of £50 million, but for those with client asset permissions it might be more appropriate at £10 million.

Q21. Do you agree with our proposed approach to moving firms between core and enhanced? If not, please explain why.

We are aware that when the regime was introduced for banks, significant support, dialogue, debate and guidance occurred between firms and the supervisory teams at the PRA. We think that such support might be beneficial from specialists within the FCA for those firms in the enhanced regime, particularly those who may be considering entering the scheme voluntarily.

Q22. Do you agree with our proposed Senior Management Functions for enhanced firms?

We would like clarification of the SMFs that enhanced firms are required to allocate regardless of whether there are currently individuals carrying out these roles. There is reference to 6 additional required SMFs yet there are 11 for firms to consider applying.

Q23. Do you agree that this will ensure the most senior people in firms are covered by the Senior Managers Regime, regardless of organisational structure? If not, please explain why.

We consider these as appropriate for mortgage and protection firms.

Q24. Do you agree with our proposals for Prescribed Responsibilities in enhanced firms? If not, please explain why.

We consider these as appropriate for mortgage and protection firms.

Q25. Do you agree with our proposal to apply the Overall Responsibility requirement to enhanced firms? If not, please explain why.

We consider these as appropriate for mortgage and protection firms.

Q26. Do you agree with our proposal to apply Responsibilities Maps to enhanced firms? If not, please explain why.

We consider these as appropriate for mortgage and protection firms.

Q27. Do you agree with our proposal to apply handover procedures to enhanced firms? If not, please explain why.

We consider these as appropriate for mortgage and protection firms.

Q28. Do you agree with our proposals for Senior Managers in EEA Branches?

No comment.

Q29. Do you agree with our proposals on the Certification Regime and Conduct Rules for EEA Branches?

No comment.

Q30. Do you agree with our proposals for Senior Managers in non-EEA branches? If you disagree, please explain why.

No comment.

Q31. Do you agree with our proposals for Prescribed Responsibilities in non-EEA branches? If you disagree, please explain why.

No comment.

Q32. Do you agree with our proposals on the Certification Regime and Conduct Rules for non-EEA Branches?

No comment.

Q33. Do you agree with our proposal to introduce a new Prescribed Responsibility for the Conduct Rules that will also apply to banking firms?

No comment.

Q34. Do you agree with our changes to the 12-week rule? If not, please explain why.

No comment.

Q35. Do you agree with our approach to applying the partner function to banking firms? If not, please explain why.

No comment.

Q36. Based on the summary above and the full analysis, do you agree with our approach and methodology for the cost-benefit analysis? If not, please explain why.

We do not understand how costs to the FCA can be described in this way. The new regime will mean even less direct supervision of firms, which does not appear to have been taken into account. We disagree with the regulatory approach that each project or piece of work that is undertaken should result in separate costs. We would expect to see the implementation of SMCR included as part of the ongoing work with industry that one would expect a regulator to carry out as part of its remit, rather than yet another extension of its current budget.

Q37. Based on the summary above and the full analysis, do you agree with our findings and conclusions for the cost-benefit analysis? If not, please explain why.

As above.