Association of Mortgage Intermediaries' response to FCA DP 23/3 Review of the Senior Managers and Certification Regime (SM&CR)

This response is submitted on behalf of the Association of Mortgage Intermediaries (AMI) and the Association of Finance Brokers (AFB). AMI is the trade association representing over 80% of UK mortgage intermediaries. AFB sits within AMI and represents second charge (formerly secured loan) brokers.

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. AMI members also provide access to associated protection products. AFB members also provide access to unsecured products.

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

Introduction

AMI is grateful to have the opportunity to respond to this discussion paper and we welcome the review of the SM&CR. We would be grateful for our comments in this section to be considered alongside our responses to the set questions.

We would like to highlight the tonal difference between the FCA/PRA discussion paper and the HMT call for evidence. We are concerned the Treasury call for evidence appears to suggest that significant reforms could be considered, which is not aligned with the FCA discussion paper as this takes a lighter touch approach.

We are aware of the HMT call for evidence on the scope, benefits and risks of the AR regime in December 2021 which discussed the option of extending SM&CR to ARs – we would be keen to hear the government's response to this and question why there has been such a significant delay in providing a response.

In our view, the SM&CR plays a valuable role and has, for the most part, worked well. Maintaining the 'status quo' could be easier for firms than a root and branch reform, even if the changes aim to simplify. We acknowledge that our perspective is predominantly as representatives of smaller firms and that 'Enhanced' firms and large banks and insurers may have contrary views. One of the great successes of SM&CR was the proportionate approach delivered via this initiative. Accordingly, it may be appropriate for any changes should reflect that success. The implementation of SM&CR was very resource intensive and we have concerns that making extensive changes to the regime at this stage is unlikely to add sufficient value. Any further changes will need to be justified, in terms of benefits and costs.

As drawn out in the introduction to the discussion paper, the main issues for firms in regards to SM&CR are often relating to the delays experienced due to the FCA authorisation team being unable to meet their SLA's in managing applications. Despite assurances on improved delivery, we continue to see issues and this risks colouring firms views of the regime.

From a trade body perspective, our view is that the clarity that the SMF roles deliver within firms has enhanced accountability and improves internal debate and decision making. There are some exceptions to this is relation to larger firms, with Boards and non-executive directors as well as larger risk and compliance functions, as lines still can be blurred.

We have considered the potential expansion of scope to cover the AR regime given the FCA's focus on the network model through the AR regime changes. We feel that this expansion would be unnecessary as APER covers this sufficiently. The enhanced requirements in the FCA's AR rules have also strengthened the regime (particularly as it takes concepts seen within SM&CR). Additionally, AR firms are unlikely to have the capabilities/knowledge/resources to understand and apply the SM&CR – this is one reason why they become an AR vs. DA. By bringing AR firms into SM&CR we think this would cloud the accountability of the principal firm and dilute their ability to execute proper systems and controls.

There is a degree of bureaucracy around the governance matrix, statements of responsibility and handover certification that might benefit from simplification. But again, now these are well established it may be less onerous for firms to maintain the status quo than adopt a new 'simplified' regime.

Questions

Q1: To what extent do you agree or disagree that the SM&CR has made it easier to hold individuals to account?

We agree that the SM&CR has provided clear role boundaries and responsibilities which allows many senior managers to be comfortable with and knowledgeable on what is required from them. However, we are concerned that implementing and amending new rules does very little to deter those determined to be rule breakers and there are little to no public enforcement outcomes to deter them.

Prior to the implementation of SM&CR there was expected to be a considerable uptick in the number of whistleblowing cases, which would support the idea that SM&CR has made it easier for anyone to hold an individual to account. This predicted increase did not materialise due in part to the substandard protections offered to whistleblowers.

AMI feels there are still inadequate protections for whistleblowers, and the consequences for SM&CR breaches may still be favourable to the professional and personal consequences of becoming a whistleblower. The FCA's own 2022 survey results show most whistleblowers find the FCA's handling of reports 'extremely or somewhat dissatisfying'. It is good to see the FCA taking further steps to address this, but we would encourage broader thinking on whistleblower protections within the context of SM&CR.

The FCA says whistleblowing 'provides the FCA with unique insights from inside the firms and markets it regulates and proposes to be more transparent with whistleblowers on how their reports were acted upon. However, this fails to acknowledge the risks individuals often take to make a report, even if done anonymously. It frames whistleblowing as merely another data source – not the result of an individual putting their reputation and career in jeopardy.

We would suggest more support and reassurance are needed along with tougher sanctions for those who break the rules, especially in respect of retaliation aimed at

suppressing/smearing the whistleblower. If individuals continue to operate in the industry after facing regulatory action for poor or unethical treatment of whistleblowers, this discourages whistleblowers from coming forward, as the potential for career damage is far greater.

Finally, we have seen limited enforcement action linked to SMF accountabilities at this time. We appreciate it takes time for cases to 'complete', but without sight of learnings, firms may currently feel that the regime is a toothless tiger. We are therefore commenting based on not seeing action for the FCA and cannot observe what may be operating within firms.

Q2: To what extent do you agree or disagree that the SM&CR regime has improved safety and soundness and conduct within firms?

We agree that the SM&CR regime has for the most part improved the safety, soundness and conduct within firms however the recent pandemic has shown that many businesses still have room for improvement in terms of operational resilience and reducing the potential harm to consumers. The introduction of Consumer Duty is likely to address some of these deficiencies.

In addition, SM&CR has enabled firms to document and quantify the high standards of safety, soundness on conduct they were already holding themselves to.

However, the on-going success of fraud and scams, indicates that regime has not yet made inroads into firms in the battle against financial crime. Evidence we see is that too much is focussed on complying with identification rules and not on transaction flow.

The requirements to undertake fit and proper and financial soundness checks assists, but we are still struggling to identify failing firms as SM&CR does not address the core factors that lead to failure.

Q3: To what extent do you agree or disagree that the fitness and propriety requirements support firms in appointing appropriately qualified individuals to Senior Manager roles?

We agree that this has helped some firms to appoint appropriate individuals. The ability of FCA to review individuals against the standards has improved the quality of candidates.

We have debated that there may be a 'blind spot' left by the lack of application to ARs, and that the recent revisions and enhancements to the regulation of AR regime may not have been needed had ARs originally been in scope. Our view remains that the disparity that exists between the DA regime under SM&CR and the Authorised Persons regime within the AR model is a difference that needs debate. Might the AR regime review have been unnecessary if SMCR had been fully embedded? Indeed, much of the new AR requirements match the fit and proper and financial soundness tests in SMCR. However, we feel that no change is required as this would dilute the systems and controls that principal firms should be applying to monitor and review their AR's.

Q4: Please provide any suggestions that can help ensure that appropriately qualified individuals are not deterred from taking up relevant Senior Manager roles.

The current requirements for evidencing actions and decisions and a perceived complexity of SMCR could be seen to be a barrier, additionally the time consuming and repetitive onboarding process could be deemed to deter people from leaving and joining new firms.

We would want to see more efficient administration of SM&CR, especially around Senior Manager onboarding and leaving processes, and the perceived complexity may be a barrier, but if enforcement of existing rules were strengthened then perhaps the obligations would seem less abstract and Senior Managers would have a clearer sense of what the regime is for? (i.e., Senior Managers may feel current regulations feel like empty bureaucracy if it's not clear why FCA wants to see evidence of action logs/decisions made).

There is also concern that a growing list of expectations on Senior Managers in relation to new and emerging risks can be off putting, we would suggest that a considered and proportionate approach is applied to any extension of responsibility such as sustainability and D&I.

Q5: To what extent do you agree or disagree that the SM&CR has made it easier for firms to hold staff to account and take disciplinary action when appropriate against them?

We agree somewhat – the clarification of role responsibilities will help identify staff that are not adhering correctly to their duties.

The honesty and integrity requirements under fitness and propriety, in theory allow firms to hold staff accountable for their impact on the company culture. However, there is minimal published evidence from the FCA/PRA to support this, and in practice, it appears that firms are struggling to link undesirable behaviours directly to an individual's role in order for it to amount to a conduct rule breach.

With regimes such as SM&CR and the ongoing implementation of Consumer Duty it is understandable that firms may concentrate on the processes and policies and overlook the importance of the people driving the change. Corporate culture can only be improved by the collective power of individuals and permissive cultures towards poor conduct are an emergent phenomenon that can be very difficult to reverse and in place cultivate a positive and safe environment.

We would welcome some collated guidance for firms on handling non-financial misconduct (as proposed in the original D&I consultation paper). The recent revelations around sexual harassment ,whistleblowing reports tripling in the last year amongst financial firms, coupled with the wider impact of the CBI allegations on the corporate world, have reinforced the need for some clear guidelines and expectations for regulated firms.

Q6: To what extent do the specific accountabilities of individual directors established by the Senior Managers Regime work in ways that complement the collective responsibility of the board of directors or decision making committees? Are there ways this could be improved?

The Management Responsibilities Map and the individual Statements of Responsibilities have clearly identified the boundaries of Senior Manager roles which ensures that all areas of responsibility are properly attributed to the relevant individual. This is effective at helping the

boards, directors and senior managers to give clarity over accountability. However, we consider there has been limited work done or sufficient guidance published by the FCA following its supervisory work on best practice here. Firms would benefit from more clarity on how to balance the demands of company law and regulatory requirements. We still consider there may be conflicts surrounding board collective responsibility, individual executive decision making and then setting these inside individual SMF prescribed elements. The demands placed on second line to deal with issues still provides challenges in the context of personal risk versus the corporate strategy. We remain concerned that in the event of enforcement proceedings, firms and key individuals may default to spending time identifying responsibility, applying blame and avoiding accountability, rather than dealing with customer issue.

Q7: To what extent do you agree or disagree that the prospect of enforcement promotes individual accountability?

We agree that prior to the implementation of SM&CR the prospect of enforcement envisaged by the industry did promote accountability, however the lack of public enforcement announcements since implementation do not instil confidence nor are they an effective deterrent. By the FCAs own admission in the FOI: Right to know request (released 22/06/2022), acknowledged that few investigations have been opened and even fewer have led to successful enforcement.

Moreover, the sluggish pace at which investigations are concluded is concerning. The recent fine levied by the FCA/PRA at the tail end of last year for issues arising in 2018 does little to inspire confidence in the investigation process. Lesson learned are still taking far too long to be published to assist good firms and inform on what is malevolent.

Q8: How could our approach to enforcement be enhanced to better support the aims of the SM&CR?

As mentioned in our response to Q7, it is difficult to comment on the approach to enforcement when we have very few examples to review. Again, utilising the FCA published FOI: Right to know request (released 22/06/2022) we can see that the number of investigations opened is an astonishingly low 120 cases for what is a substantially sized industry. The number of investigations opened since 2016 where the individual was a Senior Manager involving non-financial misconduct is four, it would be short-sighted to view these low figures as a direct result of the success of SM&CR, the data suggests that the SM&CR regime lacks the necessary enforcement to fully deliver on it intended outcomes.

Whilst we appreciate that SM&CR is at its core designed to be a preventative regime, we would expect that five years later we would have a number of enforcement cases studies to review. The lack of case studies deprives firms of valuable lessons and the length of time between incidents and the related published enforced outcomes does not suggest that this is an area of priority for the FCA/PRA.

We feel that in the absence of case studies for firms to reflect on, it would be useful for the FCA to provide guidance on what best practice looks like.

Q9: To what extent do you agree or disagree that the scope of the SM&CR is appropriate?

For the most part we agree that the scope is practical and appropriate. We feel that it would be useful for the FCA to consult with the industry to ascertain whether extending certification to cover those selling products under the Insurance Conduct sourcebook would be beneficial. We are seeing a growth in models which have protection adviser specialists selling both on an advised and non-advised basis so this might benefit from deeper consideration

We acknowledge that non-financial misconduct and its place within SMCR has been a topic of conversation recently and to reiterate our answer to Q5, we would welcome further guidance from FCA/PRA in regards to the handling of non-financial misconduct.

Q10: Are there actions the regulators could take in respect of the SM&CR that would help enhance competition or international competitiveness?

We would argue the UK's strong reputation as a centre of excellence for financial services is built on trust in its robust standards of conduct as part of its regulatory framework. We fail to see how the SM&CR regime could be simplified or substantially reworked (as the HMT paper suggests could be an option) without concomitant slackening of standards and accountability in the financial sector. Furthermore, the gaps in enforcement of SM&CR mean that in practice rogue actors are unlikely to be deterred by the presence of the regime. On the flipside, if the deficiencies in SM&CR could be addressed (particularly around administrative delays and enforcement), this may make the UK more attractive to high-calibre international firms who know their commitment to best practice and good conduct will be rewarded in a market that operates a level playing field.

Q11: To what extent do you agree or disagree that the SM&CR is applied proportionately to firms and individuals?

The regime's scaling mechanism that allows for Limited scope, Core and Enhanced firms have different roles and accountabilities is a good example of a proportionate regulatory intervention. We would welcome a similar scaling mechanism to be extended to other regulatory frameworks in the future. Our firms appreciate that the FCA achieved proportionality in this initiative.

Q12: How could the process for SMF approvals be further improved?

The process for SMF approvals continues to experience delays and despite the efforts of the FCA to reduce wait times, we understand SLA's are still not being met. We would want to see more efficient administration of SM&CR.

Alongside the approval delays, the administrative burdens in the form of repetitious/ largely irrelevant information sharing could be altered and improved upon to reduce workloads for both firms and the FCA. Some individuals under SM&CR may have to complete certification and then be responsible for renewing this certification, some of this information is also collected under the regulatory references. We are advised that many FCA information requests involve repeating information already held by or submitted to the FCA, but it is easier for the department to ask for the information again then harvest it internally. This does not give

confidence in the ability of the FCA to properly manage data on firms and their employees or AR's.

Finally, the process by which a former employee is able to gain access to records varies from firm to firm and many Senior Managers may not be aware of the process should they be subject to a regulatory investigation after the employment has been terminated. We feel that firms would welcome additional guidance from FCA on what the best practice approach would be.

Q13: To what extent to do you agree that the process for obtaining criminal records and notifying these to the regulators is effective in supporting the aims of the SM&CR?

On the whole we agree that the criminal records and notification process is effective, although many firms already conduct extensive background checks - this being a specific requirement does seem redundant and a duplication of work. This could be reduced by supplying the FCA with random samples.

Q14: To what extent do you agree or disagree that the 12-week rule sufficiently helps firms to manage changes in SMFs?

We agree that in theory the 12-week rule should help firms manage the transition period when making personnel changes but in practice it doesn't provide much tangible help due to consistent delays with FCA. It would be appropriate to consider extending past 12 weeks.

Q15: To what extent do you agree or disagree that the regulators have in place

a. **an appropriate set of Senior Management Functions to achieve the aims of the SM&CR?**
   We agree.

b. **an appropriate set of Prescribed Responsibilities to achieve the aims of the SM&CR?**
   We agree.

Q16: To what extent does the Duty of Responsibility support:

a. **personal accountability?**
   Somewhat, additional guidance could be given to make sure there is sufficient understanding of personal obligations.
b. **better conduct of Senior Managers?**
   Strongly, though the conduct covered by the duty of responsibility is covered by Senior Managers conduct rule 2, this duplication seems redundant.

Q17: To what extent do you agree or disagree that Statements of Responsibilities and Management Responsibilities Maps help to support individual accountability?

We agree that the MRM & SoR have supported individual accountability. Combined they have helped draw clear boundaries between roles and given clear guidance on responsibilities.

Conversely, the SoR can be seen to restrict some individuals, as there is a potential unintended consequence that individuals can become so concerned with adhering rigidly to the listed responsibilities that other important but not regulated aspects of their role are deprioritised.

Q18: To what extent do you agree or disagree that the Certification Regime is effective in ensuring that individuals within the regime are fit and proper for their roles?

The annual certification has allowed firms to raise the standards of what is expected from their employees in regards to competence and conduct and fosters an environment of continuous personal development.

The certification regime could be more tailored, as in its current form the scope is very broad. There is potential for it to be narrowed to roles with direct, client-facing responsibilities. This could be further enhanced by consideration of the potential for harm from the miss-selling in particular sectors. A deeper debate around the accountability of firms who decide to sell on a non-advised versus advised basis might reap dividends.

Q19: Regarding the Directory of Certified and Assessed Persons, to what extent do you agree or disagree that:

a. **it captures the appropriate types of individuals?**
   We agree somewhat, though as per our response to Q9 it does not currently capture protection only advisors as they sit outside of the certification regime and there would be merit in the FCA issuing a consultation on this to gauge the industry opinion on brining protection advisors in line with the other certified advisors.

b. **the requirements for keeping it up to date are appropriate?**
   We would disagree that the requirements are fit for purpose. It is not updated frequently enough and often data is missing or out of date. This makes it difficult to fully utilise the directory.

Q20: To what extent do you agree or disagree that regulatory references help firms make better-informed decisions about the fitness and propriety of relevant candidates?

Greater guidance on open ended questions such as *"any other information that we reasonably consider to be relevant to your assessment of whether the individual is fit and proper"* would be useful. It is currently difficult to define what could be considered a relevant response to this question.

There are still concerns that the regulatory reference requirements place firms in a difficult position if they terminate an employee who, due to their reference, is unable to find other employment. The former employee may raise a claim with an employment tribunal, regardless of the outcome and this is another potential resource burden on the firm.

Q21: To what extent do you agree or disagree that the Conduct Rules are effective in promoting good conduct across all levels of the firm?

We agree that the conduct rules and the related training are effective in creating an awareness and a deeper understanding of the practical application to an individual's role.

The addition of the new Conduct Rules in relation to Consumer Duty should also help to create the desired culture within firms.

Q22: Are there other areas, not already covered in the question above, where you consider changes could be made to improve the SM&CR regime?

There is quite a lot of overlap between bodies of regulation and in order to reduce resource burden on for both the regulators and firms, this could be made more efficient.