

Final Guidance: the Duty of Responsibility for insurers and FCA solo-regulated firms

Policy Statement

PS18/16

July 2018



This relates to

Consultation Paper 17/42
which is available on our website at
www.fca.org.uk/publications

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1 Overview

Introduction

- 1.1** This Policy Statement (PS) relates to FCA guidance on the 'Duty of Responsibility' for:
- insurance and reinsurance firms regulated by the FCA (which we call 'insurers' in the rest of this PS)
 - 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 PS)
- 1.2** In this PS, we summarise and respond to the feedback we received in reply to our Consultation Paper 17/42 (CP17/42)¹, published in December 2017. We explained in CP17/42 why we did not believe it necessary to make more than definitional amendments to our existing relevant guidance to reflect the extension of the Duty of Responsibility to insurers and FCA solo-regulated firms.

Who does this affect?

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

Context

- 1.5** As we explained in CP17/42, the Duty of Responsibility is part of the Senior Managers and Certification Regime (SM&CR). We summarised, in CP17/42, the origin, scope and features of the SM&CR, including the Duty of Responsibility, and how it will be extended to cover insurers and FCA solo-regulated firms.
- 1.6** Proposed amendments to our Handbook to reflect and implement the extension of the rest of the SM&CR were detailed in our separate CP17/25² and CP17/26³, published in July 2017 (the July CPs). We subsequently published CP17/40⁴ and CP17/41⁵, relating to the transition from the Approved Persons Regime to the extended SM&CR and associated additional proposed Handbook amendments (the Transition CPs).

1 www.fca.org.uk/publication/consultation/cp17-42.pdf

2 www.fca.org.uk/publication/consultation/cp17-25.pdf

3 www.fca.org.uk/publication/consultation/cp17-26.pdf

4 www.fca.org.uk/publication/consultation/cp17-40.pdf

5 www.fca.org.uk/publication/consultation/cp17-41.pdf



- 1.7** We are publishing this PS alongside two others. The latter PSs relate to the near final wording of those two sets of Handbook amendments and provide our responses to feedback received in reply to the July and Transition CPs. We are also publishing two guides to help insurers and FCA solo-regulated firms understand the SM&CR as it will apply to them, as well as the transition process.
- 1.8** Readers should have regard to those guides and other PSs for the detail of those amendments and their application. This PS addresses only the question whether additional amendments should be made to our Handbook to reflect the extension of the Duty of Responsibility to insurers and FCA solo-regulated firms.

Related FCA Publications

CP16/26 – Guidance on the duty of responsibility: amendments to the Decision Procedure and Penalties Manual

PS17/9 – Guidance on the duty of responsibility: final amendments (including feedback on CP16/26) to the Decision Procedure and Penalties Manual

CP17/25 – Individual Accountability: Extending the Senior Managers & Certification Regime to all FCA firms

CP17/26 – Individual Accountability: Extending the Senior Managers & Certification Regime to insurers

CP 17/40 – Individual Accountability: Transitioning FCA firms and individuals to the Senior Managers & Certification Regime

CP17/41 – Individual Accountability: Transitioning insurers and individuals to the Senior Managers & Certification Regime

CP17/42 – The Duty of Responsibility for insurers and FCA solo-regulated firms

PS18/14 – Extending the Senior Managers & Certification Regime to FCA firms - Feedback to CP17/25 and CP17/40 and near final rules

PS18/15 – Extending the Senior Managers & Certification Regime to insurers - Feedback to CP17/26 and CP17/41 and near final rules

Related PRA Publications

Supervisory Statement 28/15 – Strengthening individual accountability in banking

CP14/17 – Strengthening individual accountability in insurance: extension of the Senior Managers & Certification Regime to insurers

PS15/18 – Strengthening individual accountability in insurance: extension of the Senior Managers & Certification Regime to insurers

The Duty of Responsibility

- 1.9** The Duty of Responsibility was introduced by the Bank of England and Financial Services Act 2016 and came into force on 10 May 2016. It currently applies to FCA and PRA-approved senior managers (Senior Managers) of UK banks, building societies and

credit unions and UK bank branches of non-UK firms (collectively, deposit-takers) as well as PRA-designated investment firms⁶.

- 1.10** The Duty of Responsibility will also apply to Senior Managers of insurers and FCA solo-regulated firms when the SM&CR is extended. That extension has already been enacted but has not yet been brought into force by the Treasury.
- 1.11** The Duty of Responsibility specifies that we can take action against a Senior Manager where we can show that:
- there was misconduct by the Senior Manager's firm
 - at the time of the misconduct 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 misconduct occurred
 - the Senior Manager did not take such steps as a person in their position could reasonably have been expected to take to avoid the misconduct occurring or continuing
- 1.12** The burden of proof for all these elements lies on the FCA. The Senior Manager does not need to show that they took reasonable steps, rather it is for the FCA to prove that they did not.
- 1.13** We introduced, after public consultation, our existing Handbook guidance relating to the Duty of Responsibility, in our Decision Procedure and Penalties manual (DEPP), in May 2017.
- 1.14** In CP17/42, we explained that definitional changes proposed to our Handbook in our July CPs (as part of the wider SM&CR extension implementation) will have the effect of applying that existing DEPP guidance to Senior Managers of insurers and FCA solo-regulated firms. Those definitional changes will come into effect when the SM&CR extension is brought into force by the Treasury.

PRA guidance

- 1.15** The PRA, in its CP14/17⁷, proposed that its guidance for the application of the Duty of Responsibility to insurers would mirror its existing guidance for the application of the Duty of Responsibility to deposit-takers and PRA-designated investment firms. The PRA will be issuing its relevant PS, confirming that approach, alongside this PS.

6 The PRA's website lists deposit-takers and such investment firms:
www.bankofengland.co.uk/prudential-regulation/authorisations/which-firms-does-the-pra-regulate

7 www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/consultation-paper/2017/cp1417.pdf?la=en&hash=73F2C442B0EAF0BDACB9974BB2BB2074AA4D0483



Feedback in reply to CP17/42 and our responses

- 1.16** We received feedback in reply to CP17/42 from 14 organisations. Our responses to that feedback can be found in Chapter 2 of this PS. A full list of those respondents can be found in Annex 1 to this PS.
- 1.17** We remain of the view, having considered that feedback, that no amendments to DEPP, or the rest of our Handbook, relating to the Duty of Responsibility are necessary other than, for the avoidance of doubt, the definitional changes referred to above.

Next steps

- 1.18** The Treasury will bring the SM&CR extension, including the Duty of Responsibility, into force for insurers on 10 December 2018 and FCA solo-regulated firms on 9 December 2019.

2 Feedback in reply to Consultation Paper 17/42 and our responses

Our proposals

2.1 In CP17/42, we proposed no changes to our existing relevant Handbook guidance in DEPP, specifically in DEPP 6.2.9-A to 6.2.9-F⁸, to reflect the extension of the Duty of Responsibility to Senior Managers of insurers and FCA solo-regulated firms. We asked if respondents agreed with that proposal. This chapter sets out the feedback we received and our responses to that feedback.

2.2 The questions we asked in CP17/42 were:

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?

Feedback received

2.3 Very few respondents suggested that further relevant changes need to be made to DEPP.

2.4 A small number of respondents asked us to:

- consider whether the guidance on the Duty of Responsibility already provided in DEPP is suitable for small firms
- consider whether additional relevant guidance should be produced specifically for small firms
- define what steps are 'reasonable' for the purposes of the Duty of Responsibility
- add to that guidance basic principles of relevant compliance evidence-keeping

2.5 One respondent was concerned that the Duty of Responsibility will impose on insurers and FCA solo-regulated firms an overly onerous and unnecessary administrative burden, deter risk-taking, decision-making and applicants for Senior Manager roles, impose unforeseen and unquantifiable costs and stifle innovation.



- 2.6** The concerns described in paragraph 2.5 appear to be largely about the existence of the Duty of Responsibility, which was created by Parliament and will be applied to insurers and FCA solo-regulated firms as a result of a Treasury decision, rather than about guidance we could give about our application of it.
- 2.7** We have not therefore addressed, in our feedback responses below, the concerns described in paragraph 2.5, with one exception. That exception is the concern about administrative burden, which overlaps with the request for guidance about evidence-keeping.
- 2.8** We do not, however, believe that the Duty of Responsibility will have such a deterrent effect or stifle responsible innovation. We support such innovation⁹, including through our Regulatory Sandbox, Advice Unit and Tech Sprints.
- 2.9** The Duty of Responsibility merely requires that Senior Managers take reasonable steps. Even if they do not, no liability arises under the Duty without associated firm misconduct. Further, the burden is on the FCA to prove both the absence of those steps and the firm misconduct.
- 2.10** If the Duty of Responsibility does stifle some innovation, we believe that it does so only sufficiently and in such a way as to adequately protect consumers and markets. As we point out in the cost-benefit analysis published alongside this PS, which assesses the costs to firms of the SM&CR extension, including the extension of the Duty of Responsibility, 'innovation in financial services has not always led to improved outcomes for consumers' and 'payment protection insurance sold alongside credit was an innovation that did immense harm to consumers'.

Our responses

Small firms

Many types of firms are and will be subject to the Duty of Responsibility and there are significant differences in the size of those firms.

The Duty of Responsibility was originally created to apply, and already applies, to credit unions, along with other deposit-takers. While some deposit-takers are very large, credit unions are often very small.

Our existing relevant DEPP guidance was written with small credit unions, as well as large banks, in mind. As a result, we believe that the guidance is already flexible enough to accommodate firms of all sizes.

More specifically, the guidance already states that we will take account of all the circumstances in determining what steps we consider a person in the relevant Senior Manager's position could reasonably have taken. These include the Senior Manager's particular role and responsibilities and the scale and complexity of the relevant firm's business.

The guidance also already states that, in establishing what those responsibilities were, we will take into account, beyond statements of

9 www.fca.org.uk/firms/fca-innovate

responsibility and organisational charts, how the relevant firm operated and how responsibilities were allocated in practice.

Definition of 'reasonable'

We purposefully wrote our existing guidance so that it is flexible and non-prescriptive, takes account of all relevant circumstances and recognises that what is reasonable is context-specific and will vary according to the facts of each individual case.

The guidance already provides, in DEPP 6.2.9-E¹⁰, a lengthy and expressly non-exhaustive list of considerations we will take into account in assessing whether a Senior Manager's actions were reasonable in all the circumstances.

In addition to the points already noted above, that list includes factors we believe relevant to, for example, delegation, the establishment of reporting lines, staff appraisal processes, role transition handovers, risk identification, expansions and restructurings, external professional advice, transaction monitoring and collective decision-making.

The Duty of Responsibility will apply to a wide variety of situations, firms and Senior Manager roles within those firms. We do not believe that we can go further and specify the detail of reasonable steps by Senior Managers in different roles in each of those situations within different types of firms.

Evidencing compliance and administrative burden

The Duty of Responsibility imposes no additional obligation on a Senior Manager to explain or justify to us relevant steps they took and/or did not take, nor to keep records supporting such an explanation or justification.

As we explained in CP17/42, as noted above and as our existing relevant guidance in DEPP states, the burden of proof, in enforcing the Duty of Responsibility, lies on the FCA. We will need to show that the relevant Senior Manager did not take the steps a person in their position could reasonably have been expected to take to avoid their firm's relevant misconduct occurring or continuing.

It may, however, be in the interests of a Senior Manager to keep records of relevant steps they take, in case questions are raised, whether by their firm, its lawyers, auditors, insurers or customers, the FCA or another regulator. We do not believe it is necessary to make that general point in our DEPP guidance on the Duty of Responsibility.

Such records might be relevant not only to compliance with the Duty of Responsibility but also with our Code of Conduct for Staff sourcebook (COCON)¹¹. COCON is part of the SM&CR and requires all Senior Managers, and many other staff of firms subject to the SM&CR, to act with due skill, care and diligence.

¹⁰ www.handbook.fca.org.uk/handbook/DEPP/6/2.html

¹¹ www.handbook.fca.org.uk/handbook/COCON/2/?view=chapter



Further, any relevant FCA investigation is likely to take into account that each Senior Manager is also under a COCON obligation to take reasonable steps to make sure that the business of the firm for which they are responsible complies with the firm's record-keeping obligations imposed by our Handbook.

Our Handbook requires¹² each firm to keep records allowing us to monitor the firm's compliance. This includes compliance with its obligations under our Principles for Businesses¹³ to conduct its business with due skill, care and diligence and take reasonable care to organise and control its affairs responsibly and effectively.

For the avoidance of doubt, those COCON obligations will not, when the SM&CR is extended, be new to those individuals currently carrying out roles, at insurers and FCA solo-regulated firms, that will need, under the SM&CR, to be filled by Senior Managers.

All of those individuals are currently holders of Significant Influence Functions (SIFs) under our Statements of Principle and Code of Practice for Approved Persons¹⁴, which already require SIF holders to take such reasonable steps and act with due skill, care and diligence.

A Senior Manager's or SIF holder's failure to take reasonable steps in relation to that record-keeping by their business, which includes record-keeping in relation to their management of that business, may, quite apart from the Duty of Responsibility, amount to misconduct for which we will take disciplinary action.

We do not believe it is necessary to refer to firms' and Senior Managers' record-keeping obligations in our DEPP guidance on the Duty of Responsibility, which has not increased any administrative burden in this respect.

12 www.handbook.fca.org.uk/handbook/SYSC/9/1.html

13 www.handbook.fca.org.uk/handbook/PRIN/2/1.html

14 www.handbook.fca.org.uk/handbook/APER.pdf

Annex 1

List of respondents

Association for Financial Markets in Europe

Association of Mortgage Intermediaries

BNY Mellon

Chartered Banker Institute

European Venues and Intermediaries Association

Experian

International Underwriting Association of London

Investment Association

Legal & General

Limehouse Consulting

Personal Investment Management and Financial Advice Association

Rosediem

Tax Incentivised Savings Association

Tenet Group



Annex 2

Abbreviations used in this Policy Statement

COCON	The Code of Conduct for Staff sourcebook in the FCA's Handbook
CP	Consultation Paper
deposit-takers	UK banks, UK bank branches of non-UK firms, building societies and credit unions
DEPP	The Decision Procedure and Penalties manual in the FCA's Handbook
EU	European Union
FCA	Financial Conduct Authority
FCA solo-regulated firm	A firm regulated only by the FCA rather than also by the PRA
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
PS	Policy Statement
Senior Manager	A person approved as such by the FCA or PRA
SIF	Significant Influence Function
SM&CR	Senior Managers and Certification Regime
Transition CPs	FCA CPs 17/40 and 17/41, published in December 2017
UK	United Kingdom

We have developed the policy in this Policy Statement 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 proposals under review to assess whether any amendments may be required in the event of changes in the UK regulatory framework in the future.

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