

Policy Statement | PS22/15

# Strengthening individual accountability in insurance: responses to CP26/14, CP7/15 and CP13/15

August 2015



BANK OF ENGLAND  
PRUDENTIAL REGULATION  
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This policy statement contains the second set of final rules to implement the Senior Insurance Managers Regime for UK insurers that are within the scope of Solvency II.

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# 1 Overview

1.1 This Prudential Regulation Authority (PRA) Policy Statement (PS) provides feedback to responses to:

- those aspects of CP26/14, 'Senior insurance managers regime: a new regulatory framework for individuals',<sup>1</sup> that were not considered in PS3/15 'Strengthening individual accountability in banking and insurance – responses to CP13/15 and CP26/14'.<sup>2</sup>
- the proposals in CP7/15, 'Approach to non-executive directors in banking and Solvency II firms & Application of the presumption of responsibility to senior managers in banking firms'<sup>3</sup> in relation to Solvency II firms; and
- CP13/15, 'Changes to the Approved Persons Regime for Solvency II firms: forms, consequential changes and transitional arrangements'.<sup>4</sup>

1.2 This PS is relevant to UK insurance firms that are subject to the Solvency II Directive, third country branch undertakings, the Society of Lloyd's and managing agents ('Solvency II firms').

1.3 It sets out further final PRA rules (in addition to those published in PS3/15) to implement the Senior Insurance Managers Regime (SIMR) for Solvency II firms. Published alongside this PS is a Supervisory Statement SS35/15 that sets out the PRA's expectations of firms in relation to the new regime. The individual chapters for this supervisory statement were consulted on in CP26/14 and CP7/15.

1.4 The rules in this PS extend the basic requirement to require a reference from former employers to also cover current or former non-executive director (NED) roles. However, the PS does not contain further substantive rules on the regulatory references to be issued by a current or former employer when a firm is considering appointing a person to a senior insurance manager or NED role. On 10 June 2015, the Fair and Effective Markets Review (FEMR) issued recommendations<sup>5</sup> about the form and content of such references, and the PRA wishes to consider these recommendations further before finalising its approach to regulatory references. The PRA therefore expects to issue a further consultation on additional proposals for regulatory references later in 2015. The PRA's final rules on references will be made before the commencement of the SIMR on 7 March 2016.

1.5 The PRA is required by the Financial Services and Markets Act 2000 (FSMA) to publish a statement on the impact of rules on mutuals where the final rule differs from the draft of the proposed rule.<sup>6</sup> In the PRA's opinion, the impact of the rules as made is not significantly different from the impact of the proposed rules on mutuals.

1.6 The PRA is required by FSMA to have regard to any representations made to the proposals in a consultation, to publish an account, in general terms, of those representations and its response to them, and to publish details of any significant differences in the rules as made. There are no substantial changes to the rules on which the PRA consulted, though the

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1 Available at: [www.bankofengland.co.uk/pr/Pages/publications/cp/2014/cp2614.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/cp/2014/cp2614.aspx).

2 Available at: [www.bankofengland.co.uk/pr/Pages/publications/ps/2015/ps315.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/ps/2015/ps315.aspx).

3 Available at: [www.bankofengland.co.uk/pr/Pages/publications/cp/2015/cp715.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/cp/2015/cp715.aspx).

4 Available at: [www.bankofengland.co.uk/pr/Pages/publications/cp/2015/cp1315.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/cp/2015/cp1315.aspx).

5 Available at: [www.bankofengland.co.uk/markets/Documents/femrjun15.pdf](http://www.bankofengland.co.uk/markets/Documents/femrjun15.pdf).

6 Section 138K of FSMA.

timeframe for the submission of certain information has been extended (see Chapter 3). The account is set out as follows:

- Chapter 2 sets out feedback to responses to CP26/14 in respect of issues that were not covered by PS3/15.
- Chapter 3 sets out feedback to responses to CP13/15 regarding transitional arrangements and forms.
- Chapter 4 sets out feedback to responses to CP7/15 on the expectations of NEDs in Solvency II firms.

1.7 The final rules are set out as Appendices 1 to 3 to this statement. Appendix 4 contains the link to Supervisory Statement 35/15 '*Strengthening individual accountability in insurance*'.

## **2 Feedback to responses to CP26/14**

### **Summary of original proposals**

2.1 CP 26/14 proposed the

- the scope of the SIMR ;
- the allocation of responsibilities to senior persons;
- the application of Conduct Standards to individuals performing key functions; and
- the assessment of fitness and propriety of those individuals, including the requirement for firms to take reasonable steps to ensure the individuals performing key functions observe certain Conduct Standards.

2.2 The PRA received 22 responses from respondents, including insurers, trade bodies, and professional organisations. Rules on the majority of the issues raised were made and published in March 2015 in PS3/15. PS3/15 did not contain the Conduct Standards, nor did it contain the rules on the provision of regulatory references or any supervisory statements. This chapter sets out the responses received on these remaining issues, and describes the PRA's feedback to them and its final policy in these areas. Areas where the PRA is making some minor changes to the proposals contained in the CP are highlighted.

### **Conduct Standards**

2.3 The PRA has not made any changes to the substance of the content or scope of the Conduct Standards proposed in CP26/14.

2.4 Respondents generally supported the content of the proposed Conduct Standards. Respondents also supported the PRA's approach of applying them directly to individuals performing a Senior Insurance Management Function specified by the PRA or the Financial Conduct Authority (FCA).

2.5 The PRA acknowledges that the proposed wording of the draft rule requiring a firm to be satisfied that a person discharges a key function in accordance with the relevant Conduct Standards could have unduly implied that even a minor or suspected breach of a conduct



standard would cause them to fail this test. Therefore the wording of this rule has been amended to say that firms should consider whether a person has observed these Conduct Standards when performing an ongoing fit and proper assessment. Firms should take all reasonable steps to gather and consider information which indicates the extent to which individuals are following the relevant Conduct Standards and they should also keep a record for this assessment.

2.6 The PRA's rules state that a firm should place a requirement on all persons performing a key function to observe the relevant Conduct Standards. For key function holders (including NEDs), the PRA expects the relevant Conduct Standards to be set out in the individual's terms and conditions of engagement. For other staff performing key functions, the PRA expects the generic Conduct Standards to be promulgated in a staff handbook, or similar document. The PRA expects that the relevant Conduct Standards should also be taken into account when setting an individual's objectives each year.

2.7 The PRA cannot apply its Conduct Standards directly to notified NEDs (or to certain other key function holders) in the way that they apply to a person performing a SIMF or an FCA Controlled Function (CF). However firms are required to ensure that all persons who perform key functions, which would include all members of the board, are fit and proper on an ongoing basis; and the PRA expects firms to consider whether their NEDs (and other key function holders) have complied with the Conduct Standards as part of that assessment.

### **Regulatory references**

2.8 CP26/14 proposed that firms should have to request references before putting individuals forward for approval to perform a SIMF, and to provide references on past employees. In PS3/15 the PRA issued rules (based on the existing rule in SUP 10B of the PRA Handbook) requiring firms to take reasonable steps to obtain references as part of their assessment of a person's fitness and propriety, but did not make rules setting out the detail of the information which firms providing such a reference must include.

2.9 On 10 June 2015, the FEMR issued a number of recommendations, including in relation to the form and content of regulatory references. These recommendations reflected the considerable feedback that the FEMR received from the industry on this issue. Given this additional information, including the strong appetite from some industry participants for greater standardisation of references, the PRA has decided not to make any further rules on regulatory references at this stage and instead intends to consult on further proposals later in 2015. Subject to the outcome of this proposed consultation, the PRA expects that its final rules on references will be made before the commencement of the SIMR on 7 March 2016.

### **Supervisory statements**

2.10 There was only a small amount of feedback on the proposed supervisory statements and this largely mirrored the feedback given on the proposed rules. Where appropriate, these statements have been updated to take account of feedback to the consultations and/or the PRA's final rules and policy (as set out in PS3/15 and this PS) and to bring the relevant sections more closely in line with the corresponding Supervisory Statement 28/15 for the Senior Managers Regime (SMR)<sup>1</sup>.

2.11 The Supervisory Statement 35/15 includes a new paragraph which takes account of the FEMR recommendations. This paragraph says that the PRA expects that investment managers

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<sup>1</sup> PRA SS28/15 'Strengthening individual accountability in banking', July 2015; [www.bankofengland.co.uk/pr/Pages/publications/ss/2015/ss2815.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/ss/2015/ss2815.aspx).

and traders at insurers, who either oversee or undertake significant, or frequent, investment (or currency) activities, would normally be considered to be performing a Solvency II key function. The effect of this is that firms would then be required to:

- (i) ensure on an ongoing basis that all such individuals performing a key function are fit and proper; and
- (ii) require these individuals to observe the relevant PRA Conduct Standards.

### **3 Feedback to responses to CP13/15**

3.1 There were seven responses from respondents, including insurers and trade bodies, to the joint PRA and FCA consultation on the forms and transitional arrangements for the application of the SIMR (and the FCA's Approved Persons Regime (APR)) to Solvency II firms.

3.2 Respondents questioned the relevance or validity of some of the proposed questions in the application form (Form A) for approval of a Senior Insurance Manager, and in particular to those relating to any criminal investigations of which the firm is aware. The PRA acknowledges the concerns expressed by some respondents about the relevance of this information. Therefore some of these questions have been deleted and the PRA will consider these issues more fully in a further review of the form with the FCA. The PRA intends this will be completed before 7 March 2016. The PRA will also issue guidance to firms, on how to complete this form, before 1 January 2016.

3.3 There was also a concern expressed about the volume of possible requests for new approvals and how these would be processed within a limited timescale, particularly if some firms had difficulty in completing the proposed 'scope of responsibilities' (SoR) form. The PRA considers that completion of this form is essential for new applicants. Submission of the SoR is not a condition for grandfathering<sup>1</sup> existing senior managers under the HM Treasury Transitional Order, and only a summary needs to be included in the Solvency II governance maps to be prepared by firms and groups, and made available to supervisors (on request) from 1 January 2016. Therefore the PRA is easing the potential burden by allowing up to a further six months for firms to prepare and submit the SoR information for grandfathered individuals by 7 September 2016 at the latest. It is expected that the larger firms will be able to provide this information earlier in the year.

3.4 Similarly, firms will be allowed until 7 September 2016 to submit a notification form in respect of those 'transitional' key function holders at 1 January 2016, who are not grandfathering to a Controlled Function, nor seeking approval from the PRA for an SIMF. These are key function holders who do not need to be pre-approved by the PRA, but have to be notified to the PRA (for its assessment) in accordance with Solvency II. As noted above, a summary of the relevant information on SoRs needs to be included in the Solvency II governance maps to be prepared by firms and groups, and made available to supervisors (on request) from 1 January 2016.

3.5 The PRA was asked whether firms will be notified about the result of its assessment of a 'notified' NED (or other key function holder), and what action could be taken if the PRA had

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<sup>1</sup> 'Grandfathering' means approval to perform a senior insurance management function under section 59 of FSMA, granted pursuant to a notice required to be sent to the PRA under article 2(1) or 11(b) of the HM Treasury Transitional Order.



concerns about an individual notified to it. The PRA intends to provide a standard feedback letter to firms and, if applicable, indicate in this letter if it does not require further information on the individual at this stage. This feedback should not be taken as negating the firm's ongoing obligation to ensure the fitness and propriety of the individual, nor as constituting an assessment of suitability by the PRA. Any concerns following the PRA's assessment of the notification would be explained to the firm and both the firm and, where relevant, the individual would be expected to address such concerns.

### Transitional arrangements

3.6 The PRA proposals were based on the HM Treasury Transitional Order that provides for individuals currently approved under the Approved Persons Regime (APR) to be able to grandfather into the SIMR and perform an SIMF which is equivalent to the role they are currently approved for without requiring further approval. Respondents to the CP generally welcomed the transitional proposals for grandfathering and raised queries on the issues set out below. The PRA has not made any significant changes to its proposed approach to transitional arrangements, but is clarifying some aspects to address the queries raised and making appropriate amendments to ensure that the PRA transitional rules are consistent with the HM Treasury Transitional Order that was made on 4 March 2015.<sup>1</sup>

3.7 Individuals are eligible for grandfathering if the role they are performing (and have approval to perform) immediately before the commencement of the new regime on 7 March 2016 is an 'equivalent function' to the SIMF they wish to perform under the new regime in Table A below. The PRA's rules set out that the existing functions in Column 1 are 'equivalent' to the SIMFs that appear in the same row in Column 2 (PRA SIMFs) or Column 3 (FCA CFs).

**Table A: Equivalent functions**

Column 1	Column 2	Column 3
Pre-implementation PRA or FCA Controlled Function	PRA Senior Insurance Management Function	FCA Function
<b>UK Solvency II firm</b>		
Director (CF1)	Chief Finance function (SIMF2) Chief Risk function (SIMF4) Head of Internal Audit function (SIMF5) Chief Actuary function (SIMF20) Chief Underwriting Officer function (SIMF22) Underwriting Risk Oversight function (Lloyd's) (SIMF23) Group Entity Senior Insurance Manager function (SIMF7)	FCA Director function (CF1) (see Note)

<sup>1</sup> The Financial Services (Banking Reform) Act 2013 (Transitional and Savings Provisions) Order 2015, available at: [www.legislation.gov.uk/uksi/2015/492/pdfs/uksi\\_20150492\\_en.pdf](http://www.legislation.gov.uk/uksi/2015/492/pdfs/uksi_20150492_en.pdf).

Column 1	Column 2	Column 3
Pre-implementation PRA or FCA Controlled Function	PRA Senior Insurance Management Function	FCA Function
<b>UK Solvency II firm</b>		
Non-executive director (CF2)	Chairman (SIMF9) Senior independent director (SIMF14) Chair of the Risk Committee (SIMF10) Chair of the Audit Committee (SIMF11) Chair of the Remuneration Committee (SIMF12) Group Entity Senior Insurance Manager function (SIMF7)	Chair of the nomination committee function (CF2a) Chair of the with-profits committee function (CF2b) (see Note)
Chief executive (CF3)	Chief Executive function (SIMF1)	
Director of unincorporated association (CF5)	Chief Finance function (SIMF2) Chief Risk function (SIMF4) Head of Internal Audit function (SIMF5) Group Entity Senior Insurance Manager function (SIMF7) Chief Actuary function (SIMF20) Chief Underwriting Officer function (SIMF22) Chairman function (SIMF9) Chair of the Risk Committee function (SIMF10) Chair of the Audit Committee function (SIMF11) Chair of the Remuneration Committee function (SIMF12) Senior Independent Director function (SIMF14)	FCA Director of unincorporated association function (CF5) Chair of the nomination committee function (CF2a) Chair of the with-profits committee function (CF2b) (See Note)
FCA Apportionment and oversight (CF8)	To be dis-applied	
FCA Compliance (CF10)		Compliance (CF10)
FCA CASS Operational Oversight (CF10a)		Cass Operational Oversight (CF10a)
FCA Money Laundering Reporting (CF11)		Money Laundering Reporting Officer (CF11)

Column 1	Column 2	Column 3
Pre-implementation PRA or FCA Controlled Function	PRA Senior Insurance Management Function	FCA Function
<b>UK Solvency II firm</b>		
PRA Actuarial function holder (CF12)	Chief Actuary function (SIMF20)	
PRA With-profits Actuary (CF12A)	With-profits Actuary function (SIMF21)	
PRA Lloyd's Actuary (CF12B)	Chief Actuary function (SIMF20) Underwriting Risk Oversight function (SIMF23)	
PRA Systems and Controls (CF28)	Chief Finance function (SIMF2) Chief Risk function (SIMF4) Head of Internal Audit function (SIMF5)	
FCA Significant Management (CF29)	Chief Underwriting Officer function (SIMF22) Group Entity Senior Insurance Manager function (SIMF7) Chief Actuary function (General Insurance Firms) (SIMF20) Underwriting Risk Oversight function (Lloyd's) (SIMF23)	CF29s not otherwise approved by the PRA
FCA Customer function (CF30)		Customer function (CF30)
<b>UK Insurance Special Purpose Vehicle</b>		
Pre-implementation PRA or FCA Controlled Function	PRA Senior Insurance Management Function	FCA Function
Director (CF1)	Chief Finance function (SIMF2) Chief Actuary function (SIMF20) Group Entity Senior Insurance Manager function (SIMF7)	FCA Director function (CF1) (see Note)
Non-executive director (CF2)	Chairman (SIMF9)	Chair of the nomination committee function (CF2a) Chair of the with-profits committee function (CF2b) (see Note)
Chief executive (CF3)	Chief executive function (SIMF1)	
FCA Apportionment and oversight (CF8)	To be dis-applied	
FCA Compliance (CF10)		Compliance (CF10)
FCA CASS Operational Oversight (CF10a)		Cass Operational Oversight (CF10a)

<b>UK Insurance Special Purpose Vehicle</b>		
<b>Pre-implementation PRA or FCA Controlled Function</b>	<b>PRA Senior Insurance Management Function</b>	<b>FCA Function</b>
FCA Money Laundering Reporting (CF11)		Money Laundering Reporting Officer (CF11)
PRA Actuarial function holder (CF12)	Chief Actuary function (SIMF20)	
PRA Systems and Controls (CF28)	Chief Finance function (SIMF2)	FCA Systems and Controls function (CF28) (see Note)
PRA Significant Management (CF29)	Group Entity Senior Insurance Manager function (SIMF7) Chief Actuary function (General Insurance Firms) (SIMF20)	All CF29s not otherwise approved by the PRA
FCA Customer function (CF30)		Customer function (CF30)
<b>Third country branch undertaking</b>		
<b>Pre-implementation PRA or FCA Controlled Function</b>	<b>PRA Senior Insurance Management Function</b>	<b>FCA Function</b>
Director (CF1)	Head of Third Country Branch function (SIMF19) Chief Finance function (SIMF2) Chief Risk function (SIMF4) Head of Internal Audit function (SIMF5) Chief Actuary function (SIMF20) Chief Underwriting Officer function (SIMF22) Group Entity Senior Insurance Manager function (SIMF7)	FCA Director function (CF1) (see Note)
Non-executive director (CF2)	Chairman (SIMF9) Senior independent director (SIMF14) Chair of the Risk Committee (SIMF10) Chair of the Audit Committee (SIMF11) Chair of the Remuneration Committee (SIMF12) Group Entity Senior Insurance Manager function (SIMF7)	
Chief executive (CF3)	Head of Third Country Branch function (SIMF19)	
FCA Apportionment and oversight (CF8)	To be dis-applied	
FCA Compliance (CF10)		Compliance (CF10)
FCA CASS Operational Oversight (CF10a)		Cass Operational Oversight (CF10a)
FCA Money Laundering Reporting (CF11)		Money Laundering Reporting Officer (CF11)

Third country branch undertaking		
Pre-implementation PRA or FCA Controlled Function	PRA Senior Insurance Management Function	FCA Function
PRA With-profits Actuary (CF12A)	With-profits Actuary function (SIMF21)	
PRA Systems and Controls (CF28)	Chief Finance function (SIMF2) Chief Risk function (SIMF4) Head of Internal Audit function (SIMF5)	Systems and controls (CF28)
PRA Significant Management (CF29)	Chief Underwriting Officer function (SIMF22) Group Entity Senior Insurance Manager function (SIMF7)	Significant Management (CF29)
FCA Customer function (CF30)		Customer function (CF30)

Note: See SUP TP 7.2.3 R in the *FCA Handbook*.

3.8 Where an individual takes on new responsibilities as a result of the SIMR, including PRA Prescribed Responsibilities, this allocation of new responsibilities will not, in itself, make them ineligible for grandfathering.

3.9 The PRA recognises that, as a result of the new regime, some individuals may take on new responsibilities (or become formally responsible for areas they are already responsible for in practice) within the same SIMF. The PRA may, however, question the allocation of certain responsibilities given to senior insurance managers where they appear to be inconsistent with the overall nature and responsibilities of that function. In relation to the grandfathering of individuals, even though individuals can be grandfathered directly into an equivalent function, firms will still have an ongoing responsibility to ensure that the individual has the relevant skills and experience to perform their intended role.

3.10 However, if an individual is taking on new responsibilities that will involve them performing an SIMF which is not equivalent to the function he or she is approved to perform prior to commencement, he or she will not be eligible for grandfathering in respect of that new SIMF. Rather, a new application for approval will be required in order for the individual to be able to perform that new SIMF following commencement of the new regime. For example, a CEO who is currently approved as CF3 (Chief Executive) and who is allocated a new responsibility for overseeing the adoption of the firm's culture is eligible to grandfather into SIMF1 (Chief Executive), notwithstanding the new responsibility. But an individual who is currently approved only as CF1 (Director) and who is given the responsibility in relation to culture as part of being promoted to CEO would not be eligible for grandfathering, as CF1 (Director) is not equivalent to SIMF1 (Chief Executive).

### **The process for grandfathering**

3.11 The HM Treasury Transitional Order establishes the conditions and timing for grandfathering. Firms are required to submit their grandfathering notifications to the FCA and

PRA by 8 February 2016. Firms should submit grandfathering notifications using Form K, with one form submitted per firm<sup>1</sup>.

### **Submitting applications ahead of commencement**

3.12 The PRA recognises that firms will need to continue to recruit new individuals in the run up to commencement. For individuals who will not begin performing their role until 7 March 2016 or afterwards, the PRA and FCA will make the new application forms available from 1 January 2016 at the latest. Applications made on these new forms should not be included in the firm's grandfathering notification. Firms should note that applications for the new SIMFs can only formally be determined at the commencement date, so they should continue to apply for Controlled Functions using the existing forms for candidates whom they wish to have in place before commencement.

3.13 Where an application has been made for an existing function but has not been determined by the commencement date (a so-called 'in-flight application'), the approach set out in CP13/15 will apply. That is, the application will be treated as if it has been made under the new regime for an equivalent function as defined in Table A above. Firms will however need to include a list of any such outstanding applications on Form K, and identify the equivalent new SIMFs for each individual concerned.

3.14 One effect of the HM Treasury Transitional Order is that the statutory deadline for determining applications is suspended for applications made for existing controlled functions until a grandfathering notification is submitted in respect of that application. Notwithstanding this provision, the PRA does not intend to delay determining such applications as a matter of course. Therefore, firms should not feel compelled to submit their grandfathering notifications earlier than they would otherwise have done simply to 'restart the clock' on applications made for existing Controlled Functions.

### **Scope of responsibilities**

3.15 Firms are required to submit a SoR with each application for approval as a senior insurance manager made on or after 1 January 2016. CP13/15 contained a draft template and some proposals on how the SoR should be drafted in order to ensure that a senior insurance manager's responsibilities are set out clearly and concisely, which the PRA considers vital to the effective operation of the new regime. The SoR template should be completed so as to be practical and useable by regulators.<sup>2</sup>

3.16 The PRA's view is that a 300 word limit per responsibility should generally be sufficient, and emphasises that SoRs are primarily about recording what a senior insurance manager is responsible for, and less about how they will deliver those responsibilities. In many cases, simply allocating a PRA Prescribed Responsibility (as set out in the PRA's rules) to a senior insurance manager should suffice to identify that person clearly and formally as responsible for that area with no further elaboration required. Even where a firm adds additional responsibilities to a SoR or where the precise nature of a given senior insurance manager's responsibilities requires explanation – which will be the case with, for example, Group Entity Senior Insurance Manager – it should be possible for firms to do so in 300 words or fewer.

3.17 The PRA recognises that a Senior Insurance Manager's personal objectives, and certain details of how their responsibilities are meant to be discharged, may be contained in separate

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<sup>1</sup> In preparation for the new regime, forms are available in the dedicated Strengthening Accountability webpage on the Bank's website, see [www.bankofengland.co.uk/pr/Pages/supervision/strengtheningacc/default.aspx](http://www.bankofengland.co.uk/pr/Pages/supervision/strengtheningacc/default.aspx).

<sup>2</sup> In PS3/15 the PRA published rules setting out the 'Prescribed Responsibilities' which firms will be required to allocate to a senior insurance manager.



documents. However, this information must not dilute or undermine the Prescribed Responsibilities set out in the SoR.

### **Co-ordination with the FCA**

3.18 In the FCA's consultation in November, it proposed an overlap rule whereby if an individual was to perform an FCA governing function and was already approved to perform a PRA function (and satisfied certain other conditions), they would only need to have approval for the PRA function and the FCA function would fall away. Following further discussion on this, both regulators believe that it would be more appropriate for there to be a rule to the effect that the FCA governing function does not fall away but is included within the PRA function. The relevant individuals will need to provide information in their SoR about the FCA governing functions that they seek to perform. This overlap provision will apply both to any new individuals seeking approval from the PRA, and also for relevant individuals who are grandfathered to an equivalent PRA function while continuing to perform an FCA governing function.

3.19 The PRA believes that this will reduce the administrative burdens on firms, and will mean that both at the approval gateway and on an ongoing basis, the firm and the regulators will need to consider both functions performed by the individual when considering their fitness and propriety. This will then enable a more coherent approach to be applied.

3.20 In the FCA's CP15/16, which was issued jointly with the PRA's CP13/15, the FCA proposed to make rules which would require firms to have documents showing the scope of responsibilities for each approved person, to ensure that each person concerned is informed in writing of any change in their responsibilities, and to retain these documents, along with the governance map, for 10 years. The PRA is minded to have a similar rule, to ensure a consistent approach in relation to all approved persons and key function holders, and proposes to consult later this year.

## **4 Feedback to responses to CP7/15**

4.1 There were 10 responses received from insurers and trade associations to CP7/15. Respondents generally welcomed the PRA's proposals, and supported the underlying objectives as set out in Chapter 3 of the CP.

4.2 The CP also contained proposals in relation to banks and other 'relevant authorised persons'. This PS does not deal with the responses to those proposals, which were dealt with in PS16/15<sup>1</sup>.

4.3 The main issues that were raised in relation to NEDs for Solvency II firms came under the following headings:

- appearance of there being a two-tiered board, and impact on dynamics of board and accountability;
- differential treatment, and impact on recruitment and remuneration, for NEDs;

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<sup>1</sup> PRA PS16/15 'Strengthening individual accountability in banking: responses to CP14/14, CP28/14 and CP7/15', July 2015; <http://www.bankofengland.co.uk/pr/Pages/publications/ps/2015/ps1615.aspx>.

- potential blurring of executive and oversight activities; and
- effect on smaller mutual insurers and friendly societies.

#### **Dynamics of board and accountability**

4.4 Several respondents raised concerns that if individual NEDs have differing regulatory responsibilities, then this may impact on decision-making processes and on board dynamics. They suggested that decision-making power and focus could graduate to individuals who have more personal accountability and responsibilities, contrary to the normal collective responsibility of boards. They thought this could then lead to an erosion of effective scrutiny and collective decision making.

4.5 As SS35/15 clarifies, although the SIMR will only apply to some NEDs who will be required to take on a limited number of tailored individual responsibilities, the PRA views the regime and its application as consistent with the principle of collective decision-making underpinning unitary boards.

4.6 The individual accountability of directors in scope of the SIMR will be additional and complementary to the collective responsibilities shared by all directors under UK company law and well-established corporate governance principles, such as the Financial Reporting Council (FRC) Code. In particular, the SIMR will operate alongside the statutory and fiduciary duties of directors under UK company law including section 172(1) of the Companies Act, which requires all directors to act in the best interests of the company. All directors, irrespective of whether they are in scope of the SIMR, remain accountable under the Companies Act and, in listed firms, subject to the principles in the FRC Code on a comply-or-explain basis. In addition, all NEDs will be required to apply the Conduct Standards of integrity, due care, skill and diligence, having regard to the interests of policyholders, and disclosing appropriately any information of which the FCA or the PRA would reasonably expect to have notice.

4.7 Moreover, regardless of the fact that some NEDs will be subject to enhanced individual accountability to the PRA and FCA under the SIMR and the FCA's APR, the PRA considers it vital that the board as a whole understands the Threshold Conditions, Fundamental Rules and more detailed underlying rules in the PRA Rulebook, and establishes within the firm a culture that supports adherence to the spirit and letter of these requirements.

4.8 On 21 May 2015 the PRA published CP18/15 'Corporate Governance: Board responsibilities'<sup>1</sup>, which consults on a draft supervisory statement on the PRA's expectations of boards. The draft statement underscores the collective responsibilities shared by board members, and as such, complements the individual accountabilities introduced by the SIMR. By emphasising the collective responsibilities shared by board members, in addition to the responsibilities of individual senior insurance managers, this supervisory statement should reduce the concerns expressed by some respondents over a 'two-tier' board developing.

4.9 The PRA also recognises that, as with any major new policy initiative, it will be important to monitor the impact of the new regime, and maintain dialogue with the industry on these issues as part of understanding the effects of the policy. In its supervision of governance for firms and groups, the PRA will continue assessing the overall composition and effectiveness of boards.

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<sup>1</sup> PRA CP18/15 'Corporate Governance: Board responsibilities', May 2015; [www.bankofengland.co.uk/pr/Pages/publications/cp/2015/cp1815.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/cp/2015/cp1815.aspx). The consultation closes on 14 September 2015.

### **Potential impact on recruitment and remuneration for NEDs**

4.10 Respondents were keen to see the recruitment of high-calibre NEDs and believed it important that NEDs are drawn from a diverse range of backgrounds. Some respondents commented that many firms are already finding it difficult to appoint NEDs with the appropriate expertise. They feared that the SIMR could, ultimately, prove counter-productive if the regulatory requirements and expectations upon NEDs become overly burdensome and a disincentive to high quality candidates and diversity.

4.11 The PRA intends therefore to take a measured approach to its assessment of NEDs within the SIMR, to ensure that the regulatory objectives can be achieved without unnecessarily reducing the potential pool of NED candidates.

4.12 Accordingly, the PRA intends to assess the fitness of NEDs in scope of PRA approval only in respect of their competence for an oversight role and for being a chair, along with complementary experience or knowledge that is relevant to the remit of the committee (or board). This should not necessarily mean an expectation of greater knowledge than for those 'notified NEDs' who are members of the board but not committee chairs.

4.13 The PRA is not therefore making any change to its rules for NEDs in the SIMR in response to these comments.

### **Executive and oversight responsibilities**

4.14 Respondents requested that the regulators develop a single cohesive SIMR and APR regime that includes NEDs, but recognises their distinct challenge and oversight responsibilities. Some emphasised the need to avoid creating de facto executive responsibilities within the NED population, and to recognise that NEDs who chair committees do not take decisions in the same way as an executive director.

4.15 Some respondents believed that the risk from imposing similar regulatory requirements on NEDs as on executive directors would mean the segregation of roles become blurred or lost, and that NEDs would lose independence that is critical for the proper discharge of their role in the first place.

4.16 The PRA agrees that the roles of NEDs on boards are different from those of executive directors. In CP 18/15 the PRA stated that boards should act in a co-operative and collegiate manner whereby the non-executives support and encourage executive management and vice versa.

4.17 Moreover, the PRA agrees that all board members share in the wider board duty to promote the success of the company as well as to ensure that the regulated firm for which they are responsible continues to meet the Threshold Conditions under FSMA.

4.18 Some respondents also challenged the appropriateness of the proposed NED oversight role for remuneration policies and practices. In many firms, this oversight role will be performed through the chairmanship of a remuneration committee in the manner envisaged by paragraph 4.16 in the PRA's proposed supervisory statement in CP18/15. However, consistent with the SMR, the PRA wishes to ensure that there is adequate oversight of remuneration within firms (and groups), even where no such committee is established, by nominating a NED with this particular oversight responsibility. Accordingly, the PRA is maintaining the requirement in the SIMR for this oversight responsibility to be allocated to a NED.

4.19 However, in recognition of the comments received, the PRA has adapted the wording of this responsibility for the development and implementation of a firm's remuneration policies and practices, so that an individual NED at an insurer will only be held responsible for the oversight of remuneration policies and practices.

4.20 The PRA also received some comments relating to the proposed responsibility for oversight by a NED of the policies and procedures for whistleblowing which will be considered further in the context of the responses to proposals on whistleblowing in CP6/15<sup>1</sup>. However, in recognition of the comments received to CP7/15, the PRA has modified the wording of the whistleblowing responsibility to clarify that an individual insurance NED will be responsible for oversight of the independence, autonomy and effectiveness of the whistleblowing policies and procedures, including those for the protection of staff raising concerns, but will not be held directly responsible for the protection of staff who whistleblow.

### **Smaller insurers, mutuals, and friendly societies**

4.21 There was a concern expressed by some respondents that in order to discharge the responsibilities outlined in the consultation and ensure that independent oversight is not compromised, smaller firms may be required to engage additional NEDs which would result in significant additional costs for these firms.

4.22 It was also commented that in some mutuals, particularly smaller affinity mutuals and delegate friendly societies, there are currently member directors fulfilling 'senior manager' roles; in such cases, the organisation has continued to rely on strong input from member directors. There was a concern expressed by some respondents that, in light of the new regime, such organisations may need to consider whether to replace these NEDs with an individual with the relevant experience, and this could lead to higher costs. Moreover, it was thought by some respondents that the balance of the board might then change, and there was perceived to be a greater risk of conflict within the board due to the differences in background and expectations of NEDs.

4.23 It was suggested that one practical solution to this would be to require only the Chairman and the Chair of the Audit Committee (from the point where it becomes mandatory under the Audit Directive for insurers to have an Audit Committee) of small insurers to be treated as a Senior Insurance Manager (and hence pre-approved by PRA and subject to its conduct rules), with all other NEDs being treated as 'notified' NEDs.

4.24 Solvency II will require all in-scope insurance firms to have their NEDs (and other key function holders) assessed as being fit and proper by both the firm and the regulator. The assessment of skills expected of NEDs on the board can take account of the nature and complexity of the business. Diversity of skills and experience on the board is indeed important, and the PRA believes that its new regime will encourage and facilitate this.

4.25 Smaller insurance firms will not be required to have a full range of board committees, but if they elect to do so, then the PRA believes that it is appropriate that in light of their additional responsibilities, those NEDs who chair key board committees should be pre-approved, and should be directly subject to its conduct rules. This will be consistent also with the PRA's approach for smaller banks and building societies (as set out in PS3/15 and PS16/15). The PRA does not propose therefore to have different rules in relation to NEDs at mutual or smaller Solvency II firms.

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<sup>1</sup> PRA CP6/15 'Whistleblowing in deposit-takers, PRA-designated investment firms and insurers', February 2015; <http://www.bankofengland.co.uk/pr/Pages/publications/cp/2015/cp615.aspx>

### **Timing and process for the notification of NEDs**

4.26 The PRA does not require advance notification of planned appointments, but must be notified when the appointment is confirmed, for example when a letter of appointment is accepted. The PRA proposed in CP7/15 that the same form would be used for notifying the regulators of NEDs in banking (Capital Requirements Regulation) firms and for NEDs and other key function holders at Solvency II firms.

4.27 Firms may also, as at present, wish to have discussions with their supervisors in advance of recruiting new board members about the composition of their boards and the skills and knowledge that a new board member should possess.

4.28 Some respondents requested clarification regarding the situation where a NED who is in scope of the SIMR as a result of chairing a particular committee subsequently steps down from the chair role and thereby becomes a notified NED, and queried whether the firm would be required to submit information on the person's fitness and propriety again. The PRA confirms that such information will not be required, as the person's fitness and propriety will already have been assessed. The PRA will of course need to be notified that the person's role has changed and that he or she has ceased to perform the relevant SMF, which a firm would do by submitting Form C.

### **Criteria firms should use to assess fitness and propriety**

4.29 Firms will need to have regard to the same high-level criteria in assessing the fitness and propriety of a notified NED as they would when assessing a Senior Insurance Manager or any other key function holder. These criteria are set out in the Fitness and Propriety Part of the PRA Rulebook. The expectations of a particular individual will of course depend on the exact nature of their role; for example the Chair of the Audit Committee will be expected to have additional knowledge about audit matters which a notified NED may not require. The draft supervisory statement in CP18/15 includes an overview of the PRA's expectations regarding overall board composition. The amended PRA Rulebook also provides that in addition to obtaining references from past employers, references should also be sought from organisations where the person has held a NED role. As stated above, in the light of the FEMR, the PRA is not making new substantive rules in relation to regulatory references at this stage and intends to consult on further requirements later in the year.

### **Transitional arrangements for 'notified' NEDs**

4.30 Some respondents asked about the transitional arrangements for NEDs who are approved persons under the existing Approved Persons regime. Firms will need to notify the PRA which of their existing CF2s will be 'notified' NEDs once the SIMR comes into effect (those NEDs who will be remaining as NEDs and not performing an SIMF). This reflects the approach to grandfathering the PRA has taken for senior insurance managers. This notification should be made using Form K, the same form that firms will use to notify the PRA and the FCA of the approved persons who are becoming Senior Insurance Managers.

### **The PRA's powers in relation to 'notified' NEDs**

4.31 A number of respondents asked what action the PRA would take if it was not satisfied that a 'notified' NED was fit and proper. Generally, where the PRA has concerns about the membership of a firm's board, it would raise those concerns with the firm's Chairman, who has responsibility for the composition and functioning of the board. The PRA also has a range of other options, ranging from seeking additional information, through to use of the prohibition power in section 56 of FSMA where necessary. The PRA will consider the most appropriate course of action based on the nature, severity and urgency of its concerns.

## **5 Cost benefit analysis**

5.1 Section 138J(5) of FSMA requires the PRA to publish a cost benefit analysis of any changes to the consultation proposals which the PRA considers to be significant.

5.2 The PRA considers that the final rules published in this PS do not differ significantly from the drafts published for consultation. However, the PRA is allowing firms more time to submit certain information (as explained in paragraphs 3.3 and 3.4 above), which should ease the potential burden, and hence potential costs, for firms, relevant individuals, and itself.

5.3 In response to feedback from respondents, the PRA has sought to provide additional clarification on certain aspects of the regime in the rules, this PS and accompanying SS 35/15, which should enhance the clarity and transparency of the requirements and expectations. By doing so, the PRA promotes the effectiveness of the proposed regime through eliminating potential ambiguity and confusion, and mitigates the associated costs.



## Appendices

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- 1** PRA Rulebook: Solvency II Firms: Senior Insurance Managers Regime (No. 2) instrument 2015 available at [www.bankofengland.co.uk/pr/Pages/publications/ps/2015/ps2215.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/ps/2015/ps2215.aspx)

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  - 2** PRA Rulebook: Solvency II Firms: Senior Insurance Managers Regime – Solvency II (No.2) Instrument 2015 2015 available at [www.bankofengland.co.uk/pr/Pages/publications/ps/2015/ps2215.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/ps/2015/ps2215.aspx)

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  - 3** PRA Rulebook: Solvency II Firms: Senior Insurance Managers Regime – Technical Rules Instrument 2015 2015 available at [www.bankofengland.co.uk/pr/Pages/publications/ps/2015/ps2215.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/ps/2015/ps2215.aspx)

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  - 4** SS35/15 – Strengthening individual accountability in insurance available at [www.bankofengland.co.uk/pr/Pages/publications/ss/2015/ss3515.aspx](http://www.bankofengland.co.uk/pr/Pages/publications/ss/2015/ss3515.aspx).
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