

# The Manager-in-Charge Regime: Ruffling feathers in the year of the Rooster?

## *An Overview*

### INTRODUCTION

On 16 December 2016, the Securities and Futures Commission (SFC) [announced](#) the introduction of a Manager-in-Charge initiative (**MIC Regime**) aimed at increasing the accountability of the senior management of Hong Kong licensed corporations.<sup>1</sup>

The introduction of the MIC Regime follows the recent implementation of the Senior Managers and Certification Regime in the UK and, as with other regulators around the world, corporate governance and senior management accountability has been an increasing focus of the SFC for several years.

The SFC's intention behind the MIC Regime is to enhance, adapt, and supplement existing law and regulatory requirements imposed on the senior management of licensed corporations. The regime does not change regulatory or enforcement law, nor does it change the licensing approval regime. As noted by the SFC, “[t]hese new measures are built upon existing regulations... [they] do not seek to increase the SFC's powers.... We [the SFC] aim to heighten the awareness of Manager's-In-Charge of their obligations and liability under the law.”<sup>2</sup>

The MIC Regime, effective from 18 April 2017, requires every licensed corporation to nominate (and disclose to the SFC) at least one “manager-in-charge” (**MIC**) for each of eight designated “core functions”, including the licensed corporation's key business lines, comprising each of the activities for which the licensed corporation is licensed by the SFC, operational controls, risk management, and compliance.

This bulletin is the first in a series on the MIC Regime, in which we cover the following **key areas**:

- The MIC Regime in a nutshell
- Identifying MICs
- The role of the licensed corporation's board
- Senior management – not just MICs – obligations and liabilities
- What will be the impact on registered institutions – if any?

For a discussion of the **practical considerations for licensed corporations** when preparing for the MIC Regime, please see our bulletin “*The Manager-in-Charge Regime: Practical considerations for licensed corporations?*” available [here](#).

For more details on the **responsibilities** and **potential liabilities** for MICs (and senior management) and some **key mitigation measures**, please see our bulletin “*The Manager-in-Charge Regime: Augmenting or extending senior management accountability?*” available [here](#).

<sup>1</sup> Circular to Licensed Corporations for Augmenting the Accountability of Senior Management, 16 December 2016.

<sup>2</sup> Julia Leung, Executive Director, Intermediaries: “Manager-in Charge initiative Fostering Accountability and a compliance culture” Key note speech at AIMA APAC Annual Forum 2017 – 19 January 2017.



## THE MIC REGIME IN A NUTSHELL

<b>MICs and Core Functions</b>	<p>– A licensed corporation will be required to appoint at least one or more fit and proper individual(s) to be principally responsible, either alone or with others, for managing each of the following Core Functions:</p> <ul style="list-style-type: none"><li>– <b>Overall Management Oversight</b> (e.g. CEO, President);</li><li>– the <b>Key Business Lines</b> comprising one or more regulated activities (e.g. Head of Equity, Head of Corporate Finance, Chief Rating Analyst); <i>All regulated activity business within the Key Business Lines should have a designated MIC regardless of its infancy or financial standing.</i></li><li>– <b>Operational Control and Review</b> (e.g. COO, Head of Internal Audit);</li><li>– <b>Risk Management</b> (e.g. Chief Risk Officer, Head of Risk Management);</li><li>– <b>Finance and Accounting</b> (e.g. CFO, Finance Director);</li><li>– <b>Information Technology</b> (a function responsible for the design, development, operation, and maintenance of computer systems e.g. Head of IT);</li><li>– <b>Compliance</b> (a function responsible for setting policies and procedures for adherence to legal and regulatory requirements e.g. Head of Compliance);</li><li>– <b>Anti-Money Laundering and Counter-Terrorist Financing</b> (e.g. MLRO).</li></ul> <p>The intention is not (at least at the moment) to include persons in charge of the legal function.</p>
<b>Submission to the SFC</b>	<ul style="list-style-type: none"><li>– Certain basic information relating to each MIC (job title, Core Function(s) in respect of which he/she is responsible, and upward reporting lines) via a prescribed form (Supplement 8A).</li><li>– Organisational chart setting out the licensed corporation's management and governance structure, business and operational units, and key human resources and their respective reporting lines, including all MICs and the job titles of their report(s) and the person(s) to whom they report. Any unregulated business line needs to be noted in the organisational chart.</li></ul>
<b>Other documentation – to be submitted to the SFC on request</b>	<ul style="list-style-type: none"><li>– Board-approved document(s) setting out the detailed management structure including roles, responsibilities, accountability, and reporting lines.</li><li>– Evidence of board approval for the appointment of each initial MIC.</li><li>– An acknowledgement from each MIC of his/her appointment as a MIC and of the specific Core Function(s) for which he/she is principally responsible.</li><li>– In practice, of course, the SFC's power to require detailed information is extremely broad.</li></ul>
<b>Ongoing reporting to the SFC</b>	<ul style="list-style-type: none"><li>– A licensed corporation must notify the SFC of changes to its MICs and/or their information previously submitted to the SFC within seven business days (including an updated organisational chart where one or more MICs have changed).<sup>3</sup></li></ul>
<b>Timing</b>	<ul style="list-style-type: none"><li>– The SFC to commence the collection of MIC data from licensed corporations and corporate licence applicants on <b>18 April 2017</b>.</li><li>– The SFC expects all existing licensed corporations to have submitted their management structure information to the SFC on or before <b>17 July 2017</b>.</li><li>– By <b>16 October 2017</b> applications by Overall Management Oversight and Key Business Line MICs for approval as responsible officers (<b>ROs</b>) to be submitted, insofar as not already approved.</li></ul>

<sup>3</sup> This is consistent with the approach for directors and ROs, about whom the SFC already collects information during an application and requires changes to be notified to it under the Securities and Futures (Licensing and Registration) (Information) Rules.

## IDENTIFYING MICS

### AUTHORITY AND/OR SENIORITY?

The MIC Regime is designed to apply to senior individuals involved in the management of the business of the licensed corporation across the Core Functions. In addition to the obvious need for a MIC to be fit and proper,<sup>4</sup> the SFC has identified two criteria by which this can be assessed: a person's (i) seniority (and with that to whom they report) and (ii) apparent or actual authority in respect of the relevant Core Function.

The SFC has provided some guidance on what this might look like. A MIC should:

- have *sufficient authority* to exert significant influence on the conduct of the relevant function and make decisions (including in relation to managing resources) and manage the Core Function on a day-to-day basis; and
- be a *senior person* – i.e. expected to report directly, and be accountable, to the corporation's board of directors or to its Overall Management Oversight MIC.

The guidance raises the question as to which criterion is more important. The SFC has given no clear steer on this.

In practice, we would expect the SFC to ascribe greater importance to an assessment as to sufficient authority rather than upward reporting lines: a person of sufficient authority should naturally report up to the board or the Overall Management Oversight MIC.

If necessary, a licensed corporation may therefore need to change reporting lines to ensure that a licensed corporation's MICs report as required to the board or the Overall Management Oversight MIC. This may be in addition to reporting to a parent company or group senior management. The materials issued by the SFC imply that reporting to a parent company would not necessarily bring senior management of that company within scope for MIC purposes. However, there is no requirement that a MIC be an employee of the relevant licensed corporation or based in Hong Kong. For those managers located overseas with offshore parent companies, the position would depend, in our view, on the extent of the relationship between the onshore and offshore parties and a closer assessment of the nature of their involvement and authority in relation to the licensed corporation.

Licensed corporations will also need to consider how the requirement that a person has authority to make decisions and manage the Core Function on a day-to-day basis is to be assessed where individuals more senior than a prospective MIC also have authority over the function. In our view the SFC would accept that a person meets the MIC criteria despite the fact that aspects of the MIC's management of the Core Function, which are outside of matters that arise day-to-day, are subject to approval by other bodies or individuals. The requirement does not exclude the possibility that others within the licensed corporation may have authority as well, for example to approve a proposed strategy plan for the Core Function concerned. It is necessary to assess the interplay of existing lines of authority to the particular Core Function concerned when determining who may be the MICs.

Finally, although the SFC identifies certain titles that may suggest a person is a MIC of a particular function (for example, the Operational Control and Review MIC being a COO or Head of Internal Audit, or the Overall Management Oversight MIC being a CEO), ultimately it is the substance of a person's role and accountability within the organization by which that person's role should be judged – not their title.

<sup>4</sup> Section 129 of the SFO notes the following as areas for consideration when assessing the fitness and propriety of licensed persons:

- (a) financial status or solvency;
- (b) educational or other qualifications or experience having regard to the nature of the functions to be performed;
- (c) ability to carry on the regulated activity competently, honestly and fairly; and
- (d) reputation, character, reliability and financial integrity, and

the Code of Conduct for Persons Licensed by or Registered with the SFC and the Management and Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the SFC require all staff employed to be fit and proper to perform their duties – which would include MICs. This is reiterated in the Circular to Licensed Corporations for Augmenting the Accountability of Senior Management, 16 December 2016.



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## MIC'S RELATIONSHIP WITH THE LICENSED CORPORATION

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It is not necessary for a MIC to be employed by the licenced corporation. However, since sufficient authority within the licensed corporation is a key characteristic of a MIC, persons at a third party (i.e. not intragroup) service provider cannot be MICs (see “*Outsourcing*” in our bulletin “*The Manager-in-Charge Regime: Practical considerations for licensed corporations*”). Parent company personnel are considered above.

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## TO BE, OR NOT TO BE, A RESPONSIBLE OFFICER

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The Overall Management Oversight and Key Business Line MICs are required to be ROs. The Key Business Lines are those business activities constituting one or more types of regulated activities. Consequently, being designated as a MIC for existing ROs of regulated activities will, the SFC hopes, ensure active participation and responsibility for those directly supervising the regulated activities.

The Overall Management Oversight function is responsible for directing and overseeing the effective management of the overall operations of the licensed corporation on a day-to-day basis, including developing the business model and strategy.

However, in a number of situations individuals in this function may not meet the standard criteria (including industry experience – generally “front office” experience) set out in the SFC Guidelines on Competence to be a RO.

The SFC has acknowledged that not every Overall Management Oversight MIC will have had (recent) front office experience. It has indicated that it will consider such applicants and their experience holistically, for example by looking at the applicant’s overall career history within the industry, their proposed activities, and the resources (e.g. other ROs) available to the licensed corporation overall. In addition, the SFC has expressly acknowledged that a person who has had for some time control or operational experience in the industry (risk compliance, for example) may be a RO despite not previously having had experience of conducting a regulated activity.

We would expect the SFC to consider use of something along the lines of the “non-sole” condition, already used by the SFC in cases where a RO may not strictly meet the requisite RO criteria or are based overseas, to help it manage applicants in such circumstances and to smooth the introduction of the MIC Regime.

Unsurprisingly, this more pragmatic approach for Overall Management Oversight MICs does not extend to Key Business Line MICs.

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## HOW MANY MICS PER CORE FUNCTION?

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Where appropriate, the SFC accepts that there may be more than one MIC per Core Function, depending on a number of factors including the structure, size of the Core Function, its complexity, and/or the diversification of focus or activity. Licensed corporations may therefore wish to undertake an analysis in terms of a person’s knowledge and understanding to be a MIC of a Key Business Line, or part thereof, where the prospective MIC has not previously had significant practical experience. (See also “*Avoid Overburdening*” in our bulletin “*The Manager-in-Charge Regime: Practical considerations for licensed corporations*”).

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## MICS AND THE ROLE OF COMMITTEES

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The SFC has recognised that certain responsibilities may be held by a committee within a licensed corporation. For example, a licensed corporation may be governed by an internal management committee. However, it would still be required to designate MICs for its Core Functions. As a result, where a licensed corporation is governed by an internal management

committee, then an individual, such as the committee chairperson, must be appointed to be the MIC of the Overall Management Oversight function. In our view, similar principles would apply for other committees that hold particular responsibilities within a Core Function.

Those who are designated as a MIC cannot however delegate the responsibility and accountability that comes with that role, or authority to make decisions or the responsibility to manage the Core Function on a day-to-day basis.

Where a MIC shares responsibility with, or has delegated responsibility to, a committee or individual within the relevant Core Function, the licensed corporation should ensure that the division of responsibilities is:

- clearly understood and implemented in practice; and
- recorded in the board’s management responsibility map, committee terms of reference, and the relevant MIC’s job description.

## THE ROLE OF THE LICENSED CORPORATION’S BOARD

In the course of describing the MIC Regime the SFC highlighted the roles and responsibilities expected of the board of a licensed corporation. Many of these are general principles that apply to most companies, such as having ultimate responsibility for the affairs of a licensed corporation, including the adequacy and effectiveness of the internal control systems – including its people. Senior management, including MICs, act as the board’s delegates and therefore should be accountable to the board.

There are however a few notable, express requirements for the board in the context of the MIC Regime.

- The board must approve a formal document that clearly sets out the management structure of the licensed corporation, including the corporate roles, responsibilities (including specific responsibilities attributed to MICs as between other MICs of the same Core Function), accountability, and reporting lines of its senior management. A copy of this document must be provided to the SFC upon its request.
- The management structure of a licensed corporation – including the appointment of MICs – must be approved by its board.
- The board must ensure that each MIC has acknowledged their appointment as MIC and the specific Core Function(s) for which they are principally responsible.

## SENIOR MANAGEMENT – NOT JUST MICs – OBLIGATIONS AND LIABILITIES

Alongside the introduction of the MIC Regime, the SFC has reiterated its views on the obligations and liabilities of senior management of a licensed corporation. This is not limited to MICs. Persons comprising the senior management of a licensed corporation are its directors (including non-executive directors), ROs, and MICs and other persons involved in the management of the licensed corporation.

The obligations of senior management have long been set out in a number of the SFC’s codes and guidelines, such as the Code of Conduct for Persons Licensed by or Registered with the SFC and the Management and Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the SFC.

The introduction of the MIC Regime does not change these obligations, but it clearly brings MICs within their scope from the perspective of the SFC. MICs and other members of senior management, as relevant, must not blindly apply group decisions or policies. Instead, the MICs must consider the impact on the relevant Core Functions(s) in light of their operations and related Hong Kong regulatory requirements. If necessary the policy or decision should be modified to harmonise with those requirements.

The SFC can of course pursue senior management more generally under the Securities and Futures Ordinance, including disciplinary or criminal action, where they fail to meet the required legislative standards. For more detail on the **responsibilities** and **potential liabilities** for MICs (and senior management) and some **key mitigation measures**, please see our bulletin “*The Manager-in-Charge Regime: Augmenting or extending senior management accountability?*” available [here](#).

## WHAT WILL BE THE IMPACT ON REGISTERED INSTITUTIONS – IF ANY?

The MIC Regime does not apply to registered institutions, i.e. Hong Kong licensed banks that also carry on business in one or more regulated activities. These institutions are already subject to a “manager” regime under the Banking Ordinance. In some respects, the MIC Regime could be seen as “levelling the playing field” as between licensed corporations and registered institutions.

Despite this, we expect the Hong Kong Monetary Authority, the front-line regulator for banks, to equally focus on banks’ corporate governance, the accountability of senior management, and the appropriateness of a person to be an executive officer (in terms of seniority and authority) in a similar way to the SFC’s focus on ensuring ROs have, as a matter of fact, appropriate authority to fulfil their roles and responsibilities.

## CONCLUSION

The MIC Regime will be more than a simple form filling exercise.

The regime is at the heart of the SFC’s stated intention to hold senior management of licensed corporations to account in a more detailed way for how the business is run.

Compliance with the new regime will require careful assessment of a licensed corporation’s governance structure, personnel, and responsibilities. Arguably, the MIC Regime merely enhances the framework within which licensed corporations should already be operating, but inevitably the detailed regime will impact on licensed corporations to varying degrees regardless of their size or complexity.

It is clear that the SFC requires managers of the business to be engaged in and ultimately accountable for the function(s) they control, and non-compliance in form or substance would be taken seriously.

It is accordingly important that licensed corporations consider their existing positions and any practical steps that may be required well in advance of July 2017.

For a discussion of the **practical considerations for licensed corporations** when preparing for the MIC Regime, please see our bulletin “*The Manager-in-Charge Regime: Practical considerations for licensed corporations*” available [here](#).

If you would like further information about how Allen & Overy can assist your firm in relation to the MIC Regime, please do not hesitate to contact us.

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