payments and crypto network

Governance arrangements

A series of guides addressing the subject of governance arrangements for UK authorised Electronic Money Institutions ("EMI") and Payment Institutions ("PI").

Guidance is provided for firms and is not intended as legal advice.

Guide 4: Management information reporting

Background

UK authorised EMI and PI businesses must adhere to the regulatory requirements defined in the Electronic Money Regulations 2011 ("EMR") and the Payment Service Regulations 2017 ("PSR") as well as and associated guidance from the UK's Financial Conduct Authority ("FCA").

The EMR and PSR require firms to maintain *"robust governance arrangements"*, including *"a clear organisational structure with well-defined, transparent and consistent lines of responsibility"*, which are *"comprehensive and proportionate to the nature, scale and complexity of electronic money to be issued and payment services to be provided".*

An important part of maintaining robust governance arrangements is the ability for the Board to exercise oversight of the business, i.e. manage its operations, and make strategic decisions. These activities need to be informed by appropriate information in order to be effective. The reporting of management information to the Board is therefore a cornerstone of a firm's governance arrangements.

Oversight and decision-making responsibilities of the Board

The Board is responsible for the overall strategic direction and control of a company. They are responsible for making strategic decisions, setting company policies, and ensuring that management is acting in the best interests of the company and its shareholders. Within an EMI / PI business, this responsibility includes ensuring that the firm maintains compliance with regulatory requirements that are applicable to authorised EMI / PI. The responsibility of the Board would also include oversight of financial crime arrangements, financial performance and risk management. Ultimately, the Board is responsible for ensuring that the company is operating effectively and efficiently, and that it is able to achieve its goals and objectives. This all requires information upon which decisions can be made.

The importance of reporting management information to the Board

Reporting management information to the Board is important for a number of reasons, including:

1. **Oversight**: The Board is responsible for overseeing the management and operations of the firm. By receiving regular and appropriate management information, the Board can ensure that the firm is operating in a compliant and effective manner, and that any issues or problems are identified and addressed in a proactive and timely manner.
2. **Decision making**: The Board needs accurate and up-to-date information to make informed decisions about the firm's operations, risk management, compliance and strategic direction.
3. **Compliance**: The Board must be able to ensure that the firm maintains compliance with applicable regulations and the conditions of its authorisation. The authorisation of an EMI / PI underpins the ability of the business to provide its services and could therefore be considered the single most important 'asset' of the business.
4. **Risk management**: The Board must have a clear understanding of the firm's current risk exposure and the effectiveness of the risk mitigation controls. As part of their oversight responsibility, the Board must also be able to assess whether the risk management arrangements / framework is appropriate for the business.
5. **Accountability**: The Board is accountable to the firm's shareholders and stakeholders, and needs to provide regular reports on performance and operations. Accountability could also be considered to include the responsibility that an EMI / PI business has towards its customers (this is a key focus of the FCA, aka the Consumer Duty requirements). Accountability also extends to the FCA (e.g. in terms of reporting and notifications)
6. **Continual improvement**: The Board must work to ensure that the firm is improving its operations and adapting to the changes in the market, economy, and regulatory environment – it will do so considering reported management information. The ability to improve and adapt will be particularly important to Fintech firms where the market, competition and regulatory environment are rapidly changing.

Scope of management information to be reported to the Board

Management information reported to the Board of an EMI / PI would typically include:

1. **Financial performance**: This includes information on the firm's income, expenses, profits, and losses and would typically be reported in the form of a Profit & Loss Account, Balance Sheet and Cash Flow. Actual financial results would be compared to budget and variances explained in associated narratives. An important part of the financial reporting would be in relation to regulatory capital, specifically the capital held by the firm and the capital that is required to be held (i.e. as calculated in accordance with the prescribed method under the EMR / PSR). Financial reporting could also include information on the safeguarding reconciliations and differences corrected and monitoring metrics relevant to wind-down planning. Stress tested financial forecasts are required as part of an application for authorisation and are a good discipline to maintain once authorised.
2. **Risk management**: The Board needs to know about any potential risks to the firm, such as credit risk, market risk, or operational risk. Specific risk categories would depend on those defined in the Risk Management Framework operated by the firm and which are used to organise the risks in the Risk Register. Information on risk exposures, risk appetite, and risk management strategies should be included in the

management information. Information derived from the Risk Register would be a key source of such MI, e.g. reported in a risk ‘dashboard’.

3. **Compliance**: The Board must be able to oversee compliance with regulatory requirements, and associated guidance, and would use reported management information to support this oversight responsibility. Information reported to the Board would include information derived from the operation of the Compliance Monitoring Programme (“CMP”), regulatory examinations and reviews, internal and external audits, and any issues identified by the person responsible for day-to-day compliance operations (e.g. the Compliance Manager). Training should also be provided to the Board – MI reported to the Board could be used to support training.
4. **Operations**: Information concerning the day-to-day operations of the firm, including information on customer service, technology systems, and employee performance, will be required to monitor the performance of the business. Reports, including those prepared by internal audit, would be included in reported information together with specific reporting metrics designed to provide insight into the effectiveness and efficiency of the various operational areas.
5. **Strategic planning**: In support of strategic planning activities and decision making the Board should receive information on the firm's overall strategy and plans for growth, including information on future regulatory changes, new products, services or functionality, updates on developments in markets and competition, and the firm’s own business development activities.

<u>Board Reporting Pack</u>

Collating the information that should be reported to the Board will take a reasonable effort and it is therefore important that the Board participate in defining the scope of the MI, and the level of detail, that it requires.

A standardised ‘Board Reporting Pack’ could be used to ensure that information is provided in a pre-defined format, which includes sections for all of the important areas (as discussed above). The Board Reporting Pack would be distributed to all directors ahead of each Board meeting and discussed during the course of the meeting. Use of a standard format for the reporting of MI will help ensure consistent reporting, e.g. that the defined areas are discussed at each meeting, even if there is little to discuss. Retained Board Reporting Packs would also serve as a useful source of information for record-keeping purposes and clearly demonstrate that the Board has oversight of the firm.

The CEO would typically be responsible for ensuring that information is distributed to the Board in a timely manner, i.e. in good time before each Board meeting, such that the directors are able to review and understand the content. It is important that the directors have this information in advance in order to participate in Board discussions in an informed manner and raise questions as necessary. The CEO will need to work with other directors and senior managers in order to ensure that the required information is available and collated in time.

Information should be retained as part of the record keeping arrangements of the firm, this would include copies of the Board Reporting Package together with Agenda and Minutes.

In addition to the standard reporting cycle operated around Board meetings, directors should be able to request ad-hoc information, as necessary, in order to fulfil their oversight responsibility (of the firm as a whole as well as their particular area of responsibility). The reporting of ad-hoc information to directors would typically take place through the reporting lines defined in the staff organisation structure – see guidance in ***Applications for Authorisation Guide 3: Staff organisation structure***.

Other useful guides include:

- ***Risk Management Arrangements Guide 2: Risk management framework***
- ***Risk Management Arrangements Guide 4: Three lines of defence model; and***
- ***Compliance Arrangements Guide 3: Building a Compliance Monitoring Programme***