




Non-Financial Misconduct

Delivered by:

Peter Haines

15th July 2021



The presentation, supporting materials and the contents of this session are provided for information purposes only and do not purport to constitute legal or consulting advice. Professional legal or consulting advice should be obtained before taking or refraining from any action as a result of the contents of this document.

This meeting will be recorded.

A Quick Poll?

- Does your firm have a clearly defined method for identifying, assessing and reporting issues of non-financial misconduct?

Key References and Documents

Jon Frensham

- FCA published Decision Notice 29/3/21
- Frensham was an IFA and Director of Frensham Wealth Limited
- Decision:
 - no longer a fit and proper person
 - approval to perform his current senior management functions withdrawn
 - made an order prohibiting him from performing any functions in relation to regulated activity.

- Mr Frensham has referred the Decision Notice to the Upper Tribunal

Jon Frensham

- March 2017: Frensham was convicted of attempting to meet a child following sexual grooming. He committed this offence whilst he was an approved person. Mr Frensham was sentenced to 22 months' imprisonment, suspended for 18 months
- FCA considers that Mr Frensham is not a fit and proper person to perform any function in relation to any regulated activity

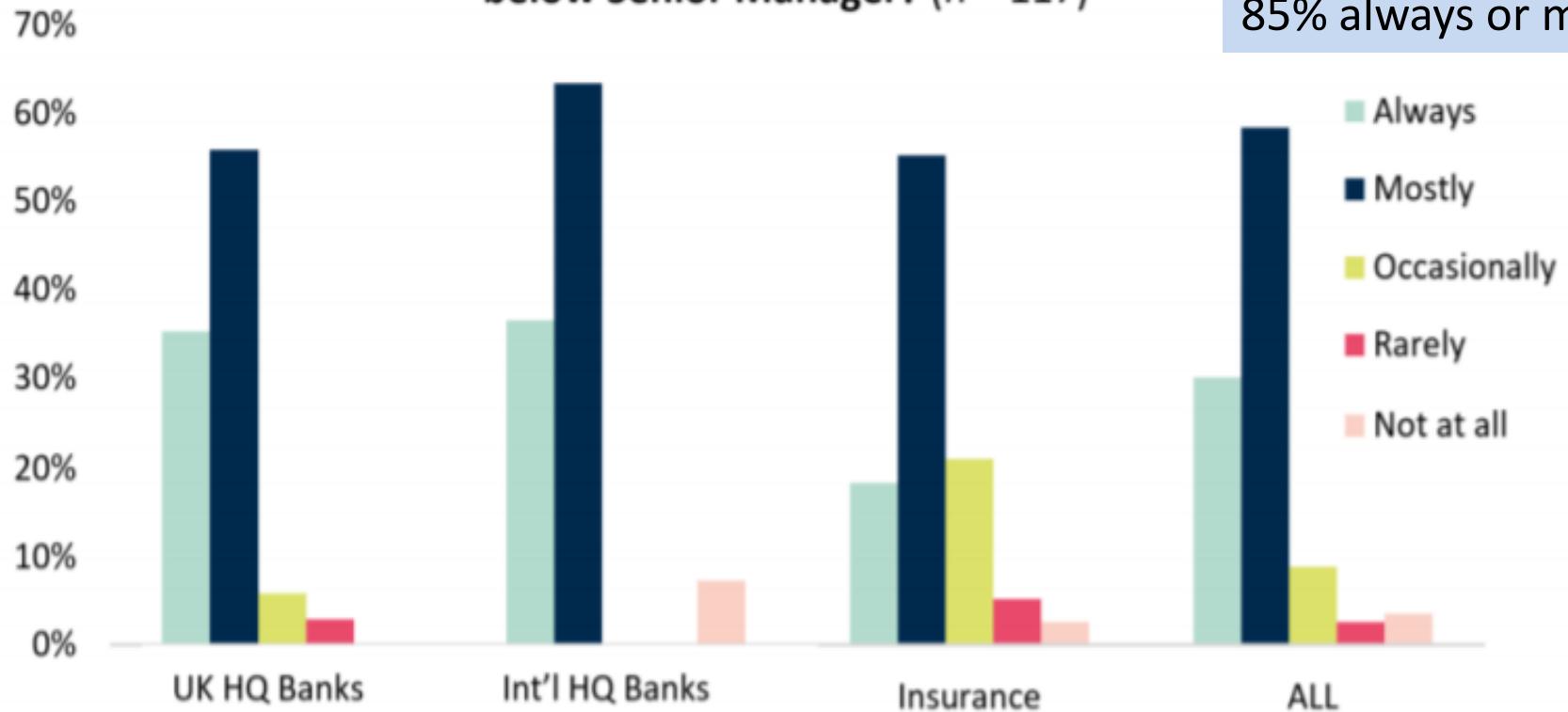
“This is because he lacks the necessary integrity and reputation.”

“The FCA considers that, as a result of this, Mr Frensham poses a risk to consumers and to confidence in the financial system. Therefore, the FCA considers it is appropriate, in order to advance its statutory objectives (which include protecting consumers and the integrity of the UK financial system), to withdraw his approval to perform senior management functions and to impose a prohibition order on him.”

PRA Evaluation of the SM&CR (December 2020)

Chart 14: Is the Certification Regime an effective mechanism for promoting improved behaviour/conduct among staff at the level below Senior Manager? (n = 117)

85% always or mostly



PRA Evaluation of the SM&CR (December 2020)

- New fitness and propriety requirements are supporting higher professional standards
- Supervisors are using the regime to clarify responsibility for new business risks and to hold senior individuals to account
- 94% of senior managers observed that the SM&CR had brought about positive changes to behaviours
- Nearly all firms reported integrating to some extent the SM&CR with internal practices
- Initial nervousness that accompanied the introduction of the SM&CR has reduced as practitioners have become familiar with it
- **Conduct notifications are being used to a limited extent only**
- It is not yet clear whether the regime is working fully as intended in conduct notifications and references.



Evaluation of the senior managers and certification regime

December 2020

FCA 2021 Disclosure Log

- Q: How many investigations has the FCA opened into non-financial misconduct in 2018, 2019 and 2020?
 - A: 2018 - 1
 - A: 2019 - 5
 - A: 2020 - 0
- Q: How many of those investigations focus on individuals classed as senior managers?
 - A: 1
- Q: How many active investigations does the FCA have into non-financial misconduct?
 - A: 1

Forsyth

➤ 30 September 2019:

- Stuart Malcom Forsyth Decision Notice
- Forsyth was CEO of Scottish Boatowners Mutual Insurance Association
- Fine of £76,180 (PRA) and £78,318 (FCA) and banned from regulated activity based on alleged tax evasion leading to a breach of Principle 1 (Integrity)
- 6th July 2021: The Tribunal overturned the FCA's and PRA's case against Forsyth

The “lack of integrity” was based on the allegation that Mrs Forsyth did no material work for SBIA, which was found NOT to be the case

“We have found that the Regulators have not made out their case that Mr Forsyth failed to act with integrity in relation to the subject matter of these references. Accordingly, we have directed that the Regulators should not impose a financial penalty on Mr Forsyth, and we have remitted the question of whether a prohibition order should be imposed to the Regulators for them to reconsider their decision in that regard. “

So Where Are We?

- The UK regulators are trying to take a stand
- The PRA has recently lost an important tribunal
- The industry is nervous...
...The regulators must be nervous too!

- A lot is being said, but...
...Arguably not much is being achieved.

- Or is it?

- **Break-Out Rooms: Has the FCA raised the bar on non-financial misconduct? If so, how?**
- **“Sta tornando a casa”**

So Where Are We?

➤ Letter from Megan Butler to the Chair of the Women and Equalities Committee of the House of Commons, September 2018:

“Culture in financial services is widely accepted as a key root cause of the major conduct failings that have occurred within the industry in recent history, and we expect firms to foster healthy cultures which support the spirit of regulation in preventing harm to consumers and markets. A culture where sexual harassment is tolerated is not one which would encourage people to speak up and be heard, or to challenge decisions. Tolerance of this sort of misconduct would be a clear example of a driver of poor culture. It would be an obstacle to creating an environment where the best talent is retained, the best business choices are made and the best risk decisions are taken.”

“Non-financial misconduct is misconduct, plain and simple” Christopher Woolard, ED of Strategy and Competition, December 2018

So Where Are We?

“An emerging theme in the last year or so has been **non-financial misconduct**, such as serious personal misbehaviour, bullying, sexual discrimination or sexual misconduct in the workplace. This type of serious misbehaviour is toxic to a working environment and can lead to bad outcomes for customers, staff, stakeholders and the firm. In our view, tolerance of this sort of misconduct would be a clear example of a driver of unhealthy culture.”

- Nausicaa Delfas, Executive Director, International at the FCA - June 2019

So Where Are We?

- Dear CEO letter: Non-financial misconduct in wholesale general insurance firms, January 2020

“As part of our approval of senior managers, an assessment of fitness and propriety will be completed. This looks at factors including competence and capability, honesty, integrity and reputation, and we will consider any known relevant issues of non-financial misconduct. In particular, a senior manager’s failure to take reasonable steps to address non-financial misconduct could lead us to determine that they are not fit and proper. We expect firms and the Boards of firms to take this into account when considering the suitability and performance of (potential) senior managers and other senior leaders.”

So Where Are We?

FCA bans three individuals from working in the financial services industry for non-financial misconduct

Press Releases | First published: 05/11/2020 | Last updated: 05/11/2020

The Financial Conduct Authority (FCA) has prohibited Russell David Jameson, Mark Horsey, and Frank Cochran from working in the financial services industry following findings that they are not fit and proper. Each of them had been convicted of serious non-financial indictable offences while working in the financial services industry.

“The FCA expects high standards of character, probity and fitness and properness from those who operate in the financial services industry, and will take action to ensure these standards are maintained.” Mark Steward

So Where Are We?

➤ Does NFM mean a breach of the Conduct Rules?

- Banks: all activity in relation to the performance of functions relating to the firm's activities
- Non-Banks: restricted to regulated activity

➤ However, can NFM involve a question over an individual's fitness and propriety (integrity and reputation)?

- The problem is that neither COCN nor FIT refer to non-financial misconduct as a basis for a decision on a breach of a conduct rule nor a lack of fitness and propriety.
- However, the various pronouncements, Dear CEO letters, speeches and enforcement actions make it clear that the regulators regard NFM as a potential lack of integrity.

Case Study

- An investment firm employs 50 Relationship Managers, whose jobs entail visiting corporate clients and then producing call reports. These reports are then filed on the firm's CRM system. Looking at the call reports, the vast majority refer to senior contacts at the clients using the expression "xxxx".
 - Have these individuals breached a conduct rule?
 - Is there a question over the individuals' fitness and propriety?
 - What would you do as the firm's Compliance Officer?

Case Study

- You work for Bank XYZ in the UK.
- You notice that a friend and colleague of yours has posted a racist comment on LinkedIn.
 - Has your friend committed a conduct rule breach?
 - Is it in relation to the firm's regulated activities?
 - Could it impact their fitness and propriety?
 - If you fail to report it, could you be committing a conduct rule breach?

Integrity and Fitness & Propriety

- Judgement in the Forsyth Case:
- “A lack of integrity does not necessarily equate to dishonesty. While a person who acts dishonestly is obviously also acting without integrity, a person may lack integrity without being dishonest. One example of a lack of integrity not involving dishonesty is recklessness as to the truth of statements made to others who will or may rely on them or wilful disregard of information contradicting the truth of such statements.”

Integrity and Fitness & Propriety

- Wingate v SRA [2018]
- “As a matter of common parlance and as a matter of law, integrity is a broader concept than honesty... . In professional codes of conduct, the term “integrity” is a useful shorthand to express the higher standards which society expects from professional persons and which the professions expect from their own members. The underlying rationale is that the professions have a privileged and trusted role in society. In return they are required to live up to their own professional standards. Integrity connotes adherence to the ethical standards of one’s own profession. That involves more than mere honesty.”

Integrity and Fitness & Propriety

- “We accept that Mr Forsyth, as the Chief Executive of a regulated insurance firm, would likewise be expected to adhere to higher standards than those expected from general members of the public because of the trust that the public rightly put in those who lead regulated financial services firms.
This is one of the ways of distinguishing “integrity” from “honesty”. The latter concept is a basic moral quality which is expected of all members of society. Honesty involves being truthful about important matters and respecting the property rights of others. It follows that a person who is dishonest in his conduct is guilty of more serious misconduct than a person who acts without integrity.
That is why regulators are usually astute in identifying whether they characterise the conduct of which they complain as demonstrating a lack of honesty as opposed to a lack of integrity.”

FCA's Five Conduct Questions

1. What proactive steps do you take as a firm to identify the conduct risks inherent within your business?
2. How do you encourage the individuals who work in front, middle, back office, control and support functions to feel and be responsible for managing the conduct of their business?
3. What support (broadly defined) does the firm put in place to enable those who work for it to improve the conduct of their business or function?
4. How does the Board and ExCo (or appropriate senior management) gain oversight of the conduct of business within their organisation and, equally importantly, how does the Board or ExCo consider the conduct implications of the strategic decisions that they make?
5. Has the firm assessed whether there are any other activities that it undertakes that could undermine strategies put in place to improve conduct?

Consider...

- A real lack of clarity here
- The regulator's expectations are clear (no), being shouted from the rooftops (yes)
- Where does this leave the people with the prescribed responsibilities?
- Consider:
 - Who decides what should be reported?
 - What is the governance over this?
 - HR? Compliance? Both?
 - Conduct Rule Breaches Committee?
 - Might this lead to fewer breaches being subject to disciplinary action?
 - Is regulation driving the HR process?
- Consider also fitness and propriety. **This also concerns more than one prescribed responsibility.**