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Non-financial misconduct: clarity from the Upper Tribunal?

September 2021

It has long been recognised that some types of non-financial misconduct (for example criminal convictions relating to offences involving dishonesty or fraud) can be so serious that they render a person not fit and proper to perform a role in the financial services sector. But in what circumstances will other types of non-financial misconduct have similar consequences? The Upper Tribunal's decision in Frensham provides important guidance.

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FCA engagement on NFM

Since at least 2018, the FCA has been highlighting the importance of non-financial misconduct as an issue of regulatory interest:

- First, certain types of non-financial misconduct (e.g., harassment or bullying in the workplace) can be an indicator of a firm's culture (including whether employees feel they have psychological safety to raise and escalate concerns);
- Secondly, non-financial misconduct can amount to a breach of the Conduct Rules, to which almost all individuals working in financial services in the UK are subject – although the conduct needs to relate to the performance of functions relating to the firm's activities (whether regulated or not); and
- Thirdly, non-financial misconduct can also be relevant to assessing whether an individual is "fit and proper" to perform a role in the financial services sector.

It is in relation to this third topic that last week's Upper Tribunal decision, Frensham v FCA[1], provides some important guidance. It has long been recognised that some types of non-financial misconduct (for example criminal convictions relating to offences involving dishonesty or fraud) can be so serious that they render a person not fit and proper. But when and in what circumstances will other types of non-financial misconduct have similar consequences?

The fit and proper test

The Financial Services and Markets Act 2000 states that, in assessing fitness and propriety, a firm (and indeed the regulators) will have regard to an individual's qualifications, training, competence and personal characteristics.

The principal criteria for assessing an individual's fitness and propriety are elaborated upon in the FCA Handbook as being the individual's:

(1) honesty, integrity and reputation;

(2) competence and capability; and

(3) financial soundness.

Non-financial misconduct will principally be relevant to (1).

Guidance in the FCA Handbook states that, in considering criminal offences, firms should consider:

- the seriousness and circumstances of the offence,
- the relevance of the offence to the proposed role,
- the individual's explanation,
- the amount of time since the offence was committed; and
- evidence of the individual's rehabilitation.

> Some types of non-financial misconduct can be so serious that they render a person not fit and proper.

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[1] [2021] UKUT 0222 (TCC).

Previous FCA decisions of interest

As noted above, there are numerous instances of the regulators prohibiting individuals on the basis of non-financial misconduct which raises serious concerns about their honesty. In addition to many cases where prohibitions have followed criminal convictions for fraudulent or other dishonest conduct, notable cases include:

- Burrows – the FCA prohibited this individual after it emerged that he had deliberately and knowingly failed to purchase a valid ticket to cover his train journey;
- Hobbs – the Upper Tribunal determined this individual should be prohibited because he had lied to and misled the FCA and the Upper Tribunal; and
- Verrier – the FCA prohibited this individual following findings by the High Court that he had engaged in an unlawful means conspiracy and had departed from the truth in his evidence.

There have, however, been a number of other cases where the FCA has imposed prohibition orders for other forms of misconduct which, whilst still serious, do not involve dishonesty:

- Flowers – the FCA prohibited this individual because of (a) his use of a work mobile telephone to call premium rate chat lines and his use of his work email account to exchange sexually explicit and otherwise inappropriate messages; and (b) his conviction for possession of illegal drugs.
- Jameson, Horsey and Cochran – most recently, in November 2020, the FCA prohibited three individuals following their convictions for serious sexual offences – offences relating to indecent images of children (Jameson), voyeurism (Horsey) and sexual assault and controlling/coercive behaviour (Cochran).

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Uncertainty following Beckwith

Shortly after the FCA published the Jameson, Horsey and Cochran decisions, the High Court issued its judgment in Beckwith v SRA[2].

In that case, the Solicitors Disciplinary Tribunal (SDT) had found that Mr Beckwith, at the time a partner at a large law firm, had inappropriately engaged in sexual activity with a junior employee, whilst the employee was heavily intoxicated and her judgment and decision-making ability was heavily impaired.

The SDT did not consider that Mr Beckwith had abused his position of seniority or authority, but nonetheless concluded that the conduct was in breach of the SRA's Principles, specifically the duties to act with integrity and in a way that maintains public trust in solicitors.

There was no allegation the sexual encounter took place without consent.

Mr Beckwith referred the SDT's decision to the High Court. The High Court found that:

- The obligation to act with integrity referenced in the Principles had to be "*drawn from and informed by*" appropriate construction of the contents of the SRA Handbook, as this was "*the best guide to the occasions and contexts where members of the solicitors' profession ought to be held to a higher standard*".
- Given the SDT had found that Mr Beckwith had not abused his position of authority and seniority and had not, therefore, taken unfair advantage of the junior employee, the SDT's finding that Mr Beckwith had "*fallen below accepted standards*" was "*not coherent*" – there were no such standards identified in the SRA Handbook.
- Whilst Mr Beckwith's conduct affected his own reputation, that did not mean that the conduct affected his own reputation as a provider of legal services or the reputation of his profession.
- Given the right to a private life under Article 8 of the ECHR, the relevant SRA Principles "*may reach into private life only when conduct that is part of a person's private life realistically touches on her practise of the profession…or the standing of the profession. Any such conduct must be qualitatively relevant*".

The Beckwith judgment understandably raised some doubt about whether the approach taken by the FCA in its recent non-financial misconduct cases was correct.

In the Frensham case, although Mr Frensham was ultimately unsuccessful, the Tribunal's views on how and when private conduct should impact on an assessment of fitness and propriety confirm that these concerns were justified.

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[2] [2020] EWHC 3231 (Admin).

The FCA's action

In March 2021, the FCA published a decision notice seeking to prohibit Jon Frensham following his conviction in March 2017 for attempting to meet a 15 year old child following sexual grooming. He was sentenced to 22 months' imprisonment, suspended for 18 months, made the subject of an indefinite sexual harm protection order and placed on the sex offenders register.

The FCA's case was that Mr Frensham's exploitation of a minor, abuse of a position of trust and deliberate and criminal disregard for appropriate standards of behaviour meant that he lacked integrity, and his prohibition was required in order to maintain public confidence in financial services.

The Upper Tribunal referral

Mr Frensham referred the matter to the Upper Tribunal for decision. He said that:

- the FCA was wrong to prohibit him because the conviction did not relate to his regulated activities;
- the conviction was not for an offence of dishonesty;
- there was no connection between the offence and his regulated activities;
- he had shown remorse for his actions; and
- prohibition was a disproportionate outcome, particularly given the length of time since the offence and the absence of evidence indicating that he presented a risk to consumers or confidence in the financial system.

Because the decision to make a prohibition order is considered a supervisory one, the role of the Upper Tribunal was not to re-determine the matter for itself, but to decide whether to dismiss the reference or to remit the matter back to the FCA giving directions to reconsider the matter in light of the Tribunal's findings of fact or law, or in relation to the matters relevant to the decision or the steps to be taken in relation to the decision.

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The Tribunal concluded that, in the context of fitness and propriety, a lack of integrity did not mean the same thing as dishonesty – somebody could lack integrity without being dishonest.

The Tribunal cited with approval Wingate v SRA[3], in which the Court observed that integrity is used as shorthand to:

> "*express the* ***higher standards which society expects from professional persons*** *and which the professions expect from their own members…Integrity connotes* ***adherence to the ethical standards of one's own profession****…Obviously, neither courts nor professional tribunals must set unrealistically high standards…The* ***duty of integrity does not require professional people to be paragons of virtue****. In every instance, professional* ***integrity is linked to the manner in which that particular profession professes to serve the public***" (emphasis added).

The Tribunal readily accepted that Mr Frensham's conduct would widely be recognised as involving a lack of integrity in the broadest sense of that term. However, consistent with Beckwith, the Tribunal said that in order to prohibit Mr Frensham, it was incumbent on the regulator to demonstrate that the behaviour engaged the "*specific standards laid down by the relevant regulator*" and was qualitatively relevant. In this regard, the Tribunal highlighted statements in the FCA's Enforcement Guide regarding its use of the prohibition power, including most notably that the FCA may use this power where it is appropriate to do so to help achieve its regulatory objectives: the relevant objectives in this case being the FCA's consumer protection and integrity objectives.

The Tribunal therefore assessed Mr Frensham's conduct by reference to the regulatory framework, and specifically the FCA's consumer protection and integrity objectives.

The key question was whether Mr Frensham's conduct in his private life "*realistically engages the question as to whether the individual poses a risk to consumers and to confidence in the financial system*".

In this regard, the Tribunal's conclusions were that:

- In relation to the consumer protection objective, the offences were unrelated to Mr Frensham's professional role, and the basis on which the FCA had sought to link his lack of personal integrity to his professional role was "speculative and unconvincing". Whilst the two FCA witnesses had asserted that his disregard of legal and ethical standards of behaviour was incompatible with holding a senior management role in a regulated firm and that there was a risk Mr Frensham would seek to exploit the trust and power that he held relative to clients, the Tribunal said that the statements were "*bare assertions*" with no evidence (e.g., criminological or psychological expert evidence) to support them. Indeed, there was no evidence that he had acted with a lack of integrity in his dealings with clients since the convictions, and the FCA had not taken any supervisory action in the four years since his conviction, suggesting that the FCA itself did not have such concerns in practice.

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[3] [2018] EWCA Civ 366.

- In relation to the integrity objective, the FCA was clearly entitled to take into account the nature of the offence and the effect it had on Mr Frensham's reputation and the reputation of the industry as a whole. However, whilst Mr Frensham's personal reputation had clearly been severely damaged and several of his clients had left following the conviction, the significant majority of his clients stayed with him. The Tribunal was not satisfied that the offence affected his reputation as a financial adviser so as to impact the integrity objective, commenting that the FCA's case would "*benefit from a more independent, analytical justification of the link between the offence and public confidence*".
- Consequently, had the Tribunal been asked to decide the case on the basis of the conviction alone, the Tribunal said it would have asked the FCA to reconsider its decision to prohibit Mr Frensham.
- However, the Tribunal found that the FCA was entitled to rely on a number of other matters, namely:
  - The fact the offence was committed in breach of bail conditions imposed on Mr Frensham following his arrest in respect of an earlier incident; and
  - Mr Frensham had failed to be open and cooperative with the FCA in relation to several matters, in failing to report: his first arrest and bail conditions; his second arrest and his remand in custody; and the fact the Chartered Insurance Institute (CII) had not renewed his Statement of Professional Standing, investigated Mr Frensham and ultimately expelled him from membership of the CII.
- These matters and Mr Frensham's attempts to justify or rationalise his actions were evidence that he had put his own interests ahead of his legal and regulatory obligations, including his obligations to be open and transparent to the regulator. Whilst Mr Frensham had continued to deal with clients in a compliant fashion and there did not appear to be a risk of him reoffending, the seriousness of his lack of candour to the regulator and the absence of genuine remorse or rehabilitation in relation to this lack of transparency meant that the Tribunal had serious concerns that Mr Frensham would continue to put his own interests above his duty of to be honest and open with the FCA. Accordingly, the Tribunal dismissed the reference, finding that these matters were sufficiently serious to justify the FCA's decision to prohibit Mr Frensham.

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4. Implications

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The Tribunal's decision effectively confirms that the approach taken in Wingate and Beckwith should also be taken in the financial services sphere. When assessing the relevance of non-financial misconduct by an individual in their private life to the individual's fitness and propriety, the regulators will need to bear in mind the following:

- Cases involving dishonesty or fraud will readily have relevance to the FCA's consumer protection and integrity objectives and to the individual's fitness and propriety;
- The mere fact that other cases of non-financial misconduct (such as serious sexual misconduct) may impact an individual's personal reputation or integrity will not necessarily mean that these matters have relevance to the regulator's standards and statutory objectives. A case by case analysis is required;
- In future, the FCA will likely need to produce much more compelling evidence to explain how such matters are both relevant to the regulator's statutory objectives and sufficiently serious to justify a prohibition. In other words, it will need to show the necessary link to justify the regulatory framework, including assessments as to fitness and propriety, reaching into conduct in an individual's private life. Bare statements by FCA staff will not be sufficient; and
- The FCA is also likely to need to consider whether it will be necessary for the it to take more urgent supervisory action in such cases, for fear that a failure to do so could be interpreted as suggesting that the conduct does not present a sufficiently significant risk to the FCA's objectives.

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5. Postscript: serious criticisms of the FCA

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The Tribunal's judgment includes some trenchant criticism of the FCA's approach to the case:

- The Tribunal noted that, at the Warning Notice and Decision Notice stage, the FCA had relied solely on the fact of the conviction, and not Mr Frensham's breach of bail conditions or lack of candour with the FCA. The Tribunal stated that, whilst the FCA was entitled to rely on new matters in the Tribunal, "*we do not regard it as entirely satisfactory that these matters did not form part of the regulatory proceedings bearing in mind that all the relevant facts were known to the Authority at the time of those proceedings. It is clearly desirable where it is possible to do so, the same case should be pleaded by the Authority before the Tribunal as it ran before the RDC*".
- There were lengthy delays in the progress of the FCA's investigation and the subsequent proceedings;
- The Tribunal criticised the FCA for putting forward evidence from a witness (a manager in the threshold conditions team) who was "*unable to deal with basic questions in cross examination*" about the FCA's approach: "*It has…not been helpful that we have not heard from those who made the relevant supervisory decisions or those who were responsible for the development of the FCA's policy regarding non-financial misconduct not related to the performance of the individual's role in financial services*";
- Perhaps most seriously, the Tribunal also said that the FCA's witnesses did not reveal until cross-examination and re-examination that one of the main reasons for the delay in the FCA taking action against Mr Frensham was that policy discussions were taking place at a senior level about the approach the FCA should take to cases of this kind. Whilst not alleging a lack of honesty or integrity by the witnesses, the Tribunal said that in this respect the FCA had "*not shown the degree of candour which the Tribunal should reasonably expect and which the Authority would expect from the firms and individuals which it regulated, which, ironically, the Authority maintains was not provided by Mr Frensham in this case*".

This is not the first occasion in recent years that the Tribunal has criticised the FCA's approach to disciplinary and non-disciplinary cases referred to the Tribunal – see, for example, the Tribunal's criticisms in Forsyth[4] of the regulators' approach to witness evidence and to disclosure (particular in relation to limitation issues), and similar comments in Hussein[5] and Burns[6]. Given the seriousness of the criticisms, the FCA will likely need to re-evaluate its approach to evidence management and to the preparation and production of factual and expert witness evidence.

> The FCA had "not shown the degree of candour which the Tribunal should reasonably expect".

[4] [2021] UKUT 0162 (TCC).

[5] [2018] UKUT 0186 (TCC).

[6] [2019] UKUT 0019 (TCC).

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