Financial Regulatory Alert

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Upper Tribunal Clarifies FCA's Powers Regarding Non-Financial Misconduct by Regulated Individuals

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Key Points

- The Upper Tribunal has issued the first ruling in relation to the FCA's decision to sanction an individual following a conviction for a criminal offence which did not involve dishonesty.
- The FCA had sought to prohibit Mr. Frensham from performing regulated activities following his conviction for a sexual offence involving a child.
- The Upper Tribunal found that Mr. Frensham's conviction was not sufficient on its own to justify the imposition of a prohibition, as the FCA had not established a sufficiently strong factual or legal basis linking the conviction itself to Mr. Frensham's lack of personal integrity as was relevant to his specific financial services role.
- This notwithstanding, the Upper Tribunal did uphold the FCA's prohibition order on alternative and narrower grounds.
- Firms are required to undertake annual reviews of all their senior managers and certified staff to determine whether they continue to be fit and proper persons. In making this assessment, firms must take into account any non-financial misconduct, and then consider whether this misconduct is linked to the individual's fitness and properness, including whether it shows a lack of integrity which is relevant to the individual's role.

Introduction

The issue of how professional regulators should respond when an individual has been accused of sexual misconduct or convicted of a sexual offence has recently been a hot topic in the UK, whether in relation to solicitors, barristers, doctors or financial services professionals.

In a recent case, the Upper Tribunal has given guidance on how the UK Financial Conduct Authority (FCA or the "Authority") must approach assessing an individual's fitness and properness to perform regulated financial services following a conviction

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for a sexual offence: see here. By extension, firms should take note of this guidance, including as part of the assessments they must make at least annually of senior managers and certified staff under the Senior Managers and Certification Regime.

In brief, the Upper Tribunal has made clear that mere conviction of a sexual offence is **not** sufficient to establish that an individual lacks the fitness and properness needed to work in the financial services sector. Rather, a conviction for a sexual offence will only be grounds for a prohibition order if there is a concrete and convincing link between that offence and the individual's lack of personal integrity as relevant to their professional role.

When assessing an individual's fitness and properness—and when considering an individual's integrity—criminal convictions are obviously important evidence to consider. The FCA, and in turn firms, must scrutinise such non-financial misconduct carefully and determine with persuasive argument whether or not the conviction does in fact affect the individual's integrity in such a way which would make them lack the fitness and properness required for the role.

Fitness, Properness and Integrity

Individuals working in the UK financial sector who perform certain functions have to be approved as "fit and proper":

- For senior managers, this approval is initially conducted by the FCA itself, and thereafter firms must assess senior managers' fitness and properness at least annually.
- Firms must assess the fitness and properness of certified staff at least annually.

As part of determining whether an individual is fit and proper, the FCA and firms need to consider whether an individual acts with the integrity required of the role.

Historically, "fitness and properness" assessments largely focused on an individual's conduct at work, particularly their technical capacity to perform the relevant role. In recent years, however, the assessment of fitness and properness has been broadened to become more holistic, with additional emphasis on an individual's conduct outside of the office and "non-financial misconduct". As Christopher Woolard, the FCA's then-Executive Director of Strategy and Competition, stated in December 2018: "[The FCA's] message to firms is clear: non-financial misconduct is misconduct, plain and simple".[1]

The FCA has recently drawn special attention to several cases where it has brought actions to prohibit individuals who have been convicted of sexual offences. Indeed, in the Enforcement Data the FCA published alongside its 2020/2021 Annual Report (on which, see our article here), one specific enforcement action was mentioned, namely the prohibition of Mark Horsey who had been convicted of voyeurism under Section 67 of the Sexual Offences Act 2003.

In many cases involving non-financial misconduct, including sexual misconduct, it is fairly clear to demonstrate that an individual lacks integrity or honesty. In Mr. Horsey's case, for example, his offence occurred in circumstances of breaches of trust, whereby he had spied on his residential tenants. Whilst the FCA's disposition of that case was fairly summary, and the decision was not referred to the Upper Tribunal, the

seriousness of the sexual offence coupled with the demonstrated breach of trust and position, served to justify prohibiting Mr. Horsey from working in the financial sector.

Mr. Frensham's Case

Jon Frensham was an independent financial adviser who was convicted of attempting to meet a child under the age of 16 following acts of sexual grooming contrary to Section 15 of the Sexual Offences Act 2003. At the time of the offence, Mr. Frensham had been on bail for a different offence.

After a significant delay in bringing any action against Mr. Frensham, the FCA sought to prohibit him from working in the regulated sector. The FCA argued that a prohibition order was appropriate because, "the nature and circumstances of Mr Frensham's offending show that he lacks integrity".[2] Further, the FCA drew attention to the fact that the offending "involved attempted exploitation of a minor, and abuse of a position of trust and a deliberate and criminal disregard for appropriate standards of behaviour".[3] As such, the FCA argued that it was necessary to prohibit Mr. Frensham "in order to maintain public confidence in the financial services industry".[4]

Mr. Frensham's counsel submitted that the FCA had failed to have regard to relevant facts, including that the conviction was unrelated to his professional activity; he was not convicted of an offence of dishonesty; and there was no connection between the offence and his professional environment (he did not work with children, for example).[5]

Based on these submissions, the Tribunal found that it was "not satisfied that a decision to make a prohibition order against Mr Frensham based solely on the fact of his conviction could have been reasonably arrived at by the Authority".[6] The Tribunal determined that the FCA's argument to connect Mr. Frensham's conviction to establish a lack of fitness and properness was based on "bare assertions" which were "based only on the awfulness of the offence itself".[7] The Tribunal stated that without additional evidentiary support to demonstrate that Mr. Frensham's criminal activity with a child was likely to lead to a "significant risk" that he would exploit other clients, the FCA's case was not made out. The Upper Tribunal repeated several times that the FCA's case was not sufficiently established on evidence.

The Upper Tribunal continued with the following summary:[8]

> "The Authority is clearly entitled to take into account the nature of the offence in considering the effect it has had on both Mr Frensham's reputation and the reputation of the industry as a whole. … But the question is whether the offence affects the reputation of Mr Frensham as a financial adviser and therefore potentially has an impact on the Authority's integrity objective. Furthermore … popular outcry is not proof that a particular set of events gives rise to any matter falling within a regulator's remit."

This paragraph may be contrasted with statements by the FCA on this topic, including, for example, a letter to the Chair of the Parliamentary Women and Equalities Committee, in which Megan Butler (then the FCA's Executive Director of Supervision) stated firmly: "we view sexual harassment as misconduct which falls within the scope of our regulatory framework".[9] In effect, the Upper Tribunal in this judgment has drawn the FCA back from an overbroad view of its "regulatory framework".

In the context where the FCA has recently announced its intention to "test [its] powers to the limit",[10] and the FCA is proposing its decision making process to allow it to make "bolder" decisions (in relation to which, see our article here), it is perhaps an unwelcome reminder to the FCA that the Upper Tribunal is able to, and prepared to, keep the regulator within its statutory bounds.

Outcome of Mr. Frensham's Case

Notwithstanding that the Upper Tribunal disapproved of the FCA's primary reasoning based on his conviction, the Tribunal found on this record that there was an alternative basis upon which a prohibition order could be imposed on Mr. Frensham. In this case, this related to other facts surrounding the offence, including that:

- It was committed whilst he was on bail.
- He had failed to be open and transparent with the Chartered Insurance Institute (CII) (of which he had been a member, and was later expelled).
- He had failed to be open and transparent with the FCA when the CII had not renewed his Statement of Professional Standing which was a fundamental requirement for him to be able to carry on his business CII).
- He had failed to show genuine remorse.

As such, whilst on different and narrower grounds, the Upper Tribunal agreed that there was a lawful basis upon which a prohibition order could be imposed.

Commentary

The FCA appears to have approached this case as if it were "straightforward".[11] Indeed, the FCA was strongly criticised by the Tribunal for the way in which it presented this case, with in one instance the Tribunal commenting:[12]

> "We regret to say that in this respect the Authority has 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 regulates, which, ironically, the Authority maintains was not provided by Mr Frensham in this case."

As appears to have been the FCA's view, many people may instinctively think that this case is simple, on the basis that they think it should be self-evident that someone convicted of a serious sexual offence regarding a child is not fit and proper to hold a professional role in the financial services sector. The lesson of this case is that these sorts of instinctual reactions are not the correct legal approach, even if—ultimately—it may be rare that someone with such a criminal record will satisfy the fitness and properness requirements.

As stated above, as part of the Senior Managers and Certification Programme, at least once a year, firms have to assess whether their senior managers and certified staff are fit and proper persons. This includes assessing any instances of non-financial misconduct, including alleged or proved sexual misconduct. Firms should also recall that where they discover instances of misconduct—including non-financial misconduct—they may be required to disclose this to the FCA in accordance with the obligation to be open and co-operative with the regulator.

Where non-financial misconduct has a direct connection to the individual's role—for example, if an individual sexually harasses a colleague—it is usually fairly straightforward to demonstrate why the individual does not have the requisite integrity for their professional role.

Where the non-financial misconduct is not directly connected to an individual's position—including that it takes place away from the office—then firms will have to look harder at whether or not the conviction impugns the individual's integrity in such a way that they cease to satisfy the fitness and properness requirements. In such circumstances, firms should be careful not to rely on assumptions or bare assertions in stating that someone lacks fitness and properness.

Firms should also be mindful of the circumstances around the offence—including whether the individual was open and candid with the firm about the offence, and whether or not he/she showed remorse—to consider whether or not these factors also impact the individual's integrity in a relevant manner. For example, an individual who has hidden or downplayed misconduct may lack the integrity required to be a fit and proper person.

[1] https://www.fca.org.uk/news/speeches/opening-and-speaking-out-diversity-financial-services-and-challenge-to-be-met.

[2] - https://assets.publishing.service.gov.uk/media/612e14dfe90e07054107585e/Frensham_v_FCA.pdf ("*Frensham*"), paragraph 4.

[3] *Frensham*, paragraph 4.

[4] *Frensham*, paragraph 5.

[5] *Frensham*, paragraph 7.

[6] *Frensham*, paragraph 174.

[7] *Frensham*, paragraphs 182 and 183.

[8] *Frensham*, paragraph 185.

[9] https://www.fca.org.uk/publication/correspondence/wec-letter.pdf, page 1.

[10] https://www.fca.org.uk/news/speeches/transforming-forward-looking-proactive-regulator.

[11] Indeed, one of the witnesses proffered by the FCA during the Upper Tribunal hearing was the manager of the team which "deals with straightforward Threshold Conditions cases": see Frensham, paragraph 76.

[12] *Frensham*, paragraph 81.

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