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By email to: cp17-25@fca.org.uk
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Dear Sir/ Madam

CP17/25 Individual accountability: extending the Senior Managers and Certification Regime (SM&CR) to all FSMA authorised firms and CP17/26 Individual accountability: extending the SM&CR to insurers

This is the Financial Services Consumer Panel's response to CP17/25 Individual accountability: extending the Senior Managers and Certification Regime (SM&CR) to all FSMA authorised firms and CP17/26 Individual accountability: extending the SM&CR to insurers¹.

The Panel supports the FCA's strategic focus on strengthening individual accountability across the industry, and the SM&CR is a positive step. However, we would like to see the proposed changes to governance and culture lead to measurable improvement in the outcomes for consumers.

We would like to offer the following observations and proposals:

The FCA must address the risk of group-think in boardrooms

- These consultations are a missed opportunity for the FCA to send a strong message to firms about good governance. The Panel remains concerned about the lack of diversity on boards across the industry. The symptoms of "group think" - the deterioration of mental efficiency, reality testing and moral judgement that is the result of in-group pressures² - were all too apparent in the 2008 banking crisis. Boards and senior executives of financial institutions were excessively optimistic and took too many risks. They failed to listen to warnings, or to question their own stances on ethical issues. There was no challenge to business models that were flawed from a consumer perspective. Academic research demonstrates that group think is exacerbated by board homogeneity. Board homogeneity is perpetuated when advertisements for new board members invite applications from those who already have the same kind of board

¹ The Panel separately responded to the Bank of England PRA Consultation Paper – CP8/17 Strengthening accountability in banking and insurance: optimisations to the SIMR, and changes to SMR forms, July 2017. This is available at https://www.fs-cp.org.uk/sites/default/files/fscp_response_pra_board_diversity.pdf

² Janus, I.L. (1972) Victims of Groupthink: A Psychological Study of Foreign Policy Decisions and Fiascos, Houghton-Mifflin, Boston

experience. When the FCA assesses the governance of firms under the new regime, it should take into account the composition of boards, and the diversity of senior executives and teams.

- The FCA should review whether its “fit and proper” requirements support the recruitment of diverse candidates into leadership positions in firms and assess whether the requirements manage the detrimental effects of group-think.

Embedded conflicts of interests and individual accountability

- The imposition of a “duty of responsibility” on individuals who pose a risk of significant harm to a firm and its customers is right. However, the FCA should not underestimate the embedded conflicts that executives and management have in their day to day work. They must balance a corporate framework designed to generate profits (often in vertically integrated business models and value chains) against the interests of consumers. Strategy, governance, culture and attitude to consumers should be aligned. The FCA should include a Prescribed Responsibility for a senior individual to assess and report this alignment on a regular basis.
- We do not agree with the FCA that development of culture should not be a prescribed individual responsibility ‘on the basis that culture is the responsibility of the whole firm’³. Something that is everyone’s responsibility means nobody has to take responsibility. Culture drives behaviour. There needs to be an individual who is responsible for reporting specific culture indicators in a firm and whether those indicators support good customer outcomes.
- The Head of HR should be specified as a significant function because this role is in a unique position to monitor alignment of firm incentive schemes, performance appraisals and hiring processes.
- Institutions with a global footprint and matrix reporting structures risk a repeat of the 2008 financial crisis. The culture and governance structures of firms with headquarters and senior staff located outside of the UK pose greater risks to customer protection. The SM&CR territorial limitation should be extended beyond just those individuals who ‘deal with clients’ to include those who are engaged in the development and execution of strategy.
- We agree with the proposal to include an assessment of value for money as a Prescribed Responsibility. This should require individuals to challenge how business models deliver value for consumers, but the FCA could usefully provide guidance on how to do this. The value for money factors set out in the FCA Asset Management Market Study final report may be a helpful starting point for guidance to individuals on how they might go about assessing whether their business practices offer value for money for consumers.

FCA Support for whistleblowers

- At the same time as it extends the SM&CR, the FCA should improve regulatory support for whistle-blowers. Individuals must have confidence that they will not face financial and professional ruin when they report bad practices which are carried out at firms.

Yours faithfully

Sue Lewis
Chair, Financial Services Consumer Panel

³ Section 3.62 of CP17/26