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# Non-Financial Misconduct reassessed in light of *Frensham v The Financial Conduct Authority*. If in doubt, disclose!

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## Introduction

- The UK Financial Conduct Authority (the "**FCA**") issued a prohibition order against Mr Frensham based on his conviction for an offence which did not involve financial fraud or dishonesty and was unrelated to regulated activity. Following a referral, the Upper Tribunal considered such a prohibition for the first time in *Frensham v The Financial Conduct Authority [2021] UKUT 0222 (TCC)*.

- Although the Tribunal concluded that the conviction alone was insufficient to make a prohibition order, the FCA's decision was nonetheless upheld due to Mr Frensham's failure to be open and transparent with the FCA during the course of the criminal investigation and later regulatory proceedings brought by the Chartered Insurance Institute ("**CII**"), which meant that he lacked integrity.

- In short, the Tribunal concluded that "*it is not the fact that a criminal offence has been committed that is fatal to an applicant's case but the manner in which he deals with the consequences that follow. In this case, we have found that the way Mr Frensham dealt with those consequences demonstrated a lack of integrity which entitles the Authority to exercise the prohibition power in order to further its statutory objectives*".

- The Tribunal's carefully reasoned judgment provides essential guidance both to the FCA and to firms assessing an individual's fitness under the Senior Managers and Certification Regime ("**SMCR**") and more generally under the Individual Conduct Rules ("**COCON**"), on how non-financial misconduct committed in an individual's private life, where unrelated to their regulated activity, should be approached. We analyse some of these key lessons at the end of this note.

## The Facts

Jon Frensham was the sole approved person and majority shareholder of a financial advisory firm. In March 2016, he was arrested for attempting to sexually groom a person under the age of 18. He was released on bail and was not subsequently charged with an offence. In September 2016, he was again arrested for a grooming offence in relation to a person he believed to be 15 years old. Pending trial, he was remanded in custody for breach of his bail terms. Mr Frensham did not disclose either the arrest or his imprisonment to the FCA. Rather, a member of the public informed the FCA of his arrest. Correspondence with the FCA followed (while he was in prison) in which Mr Frensham told the FCA that his wife was handling all correspondence and that a locum (another professional in the same field) was in place to deal with clients.

The FCA agreed to allow the firm to carry on business. Mr Frensham was reminded of his obligations under Principle 11[1] and the requirement for regulated firms to maintain clear communications with the FCA.

In March 2017, after pleading not guilty and giving evidence in his defence, Mr Frensham was convicted by a jury. He was given a suspended sentence and released from custody (and kept the FCA informed of the position). In light of the adverse publicity around his conviction, Mr Frensham changed both his name and that of the firm and continued to act as a regulated financial adviser.

In January 2019, the FCA enforcement team wrote to Mr Frensham to inform him of their recommendation to the Regulatory Decisions Committee ("**RDC**") to make a prohibition order. In October 2020, a Decision Notice was issued prohibiting Mr Frensham from performing activities. The Decision Notice was issued on the basis that: (i) his lack of integrity was at odds with his role as a financial adviser; (ii) he had harmed public confidence in the financial services industry; and (iii) he had failed to be transparent. Mr Frensham referred the FCA's decision to the Upper Tribunal.

## The Law

The FCA may withdraw approval under Section 63 of the Financial Services and Markets Act 2000 in relation to the performance of a function if it considers that a person is not fit and proper to perform the approved function. The judgment contains a useful summary of the applicable legal and regulatory provisions around the Fit and Proper Test (the "**FIT test**") (and summarised in our C&G briefing here) and the relevant authorities. The principal relevant consideration under the FIT test was whether Mr Frensham lacked integrity or requisite reputation to continue to undertake regulated activities.

Given this was a novel reference, the Tribunal grappled with how to approach integrity. As Mr Frensham had not been dishonest, the question was whether regulatory action was justified on the basis that his failure to act with integrity in his personal life engaged the specific standards laid down by the FCA. Although FIT 2.1.3G lists being convicted of a criminal offence as a relevant consideration in the FIT test, it does not always mean a person is no longer fit and proper.

Drawing on recent authorities in the solicitors' field and especially *Beckwith v SRA [2020] EWHC 3231 (Admin)*, the Tribunal established five principles that should be applied to professional activities regulated by the FCA:

(i) Integrity means adherence to the ethical standards of the profession concerned, in this case acting as an independent financial advisor;

(ii) Professionals may be held to a higher standard than the general public, although they are not required to be paragons of virtue;

(iii) Public trust in professional services permits some scrutiny of a person's private affairs;

[1] Principle 11 includes a requirement for a firm to disclose to the FCA appropriately anything relating to the firm of which the FCA would reasonably expect notice. SUP 15 provides guidance on the type of event or change in condition which a firm should consider notifying in accordance with P11. There are various provisions that may be applicable in the reporting of non-financial misconduct such as a breach of COCON (see SUP 15.11). In addition, SUP 15.3.17, states that a firm must notify the FCA if it "*suspects that one of its employees may be guilty of serious misconduct concerning his honesty or integrity and which is connected with the firm's regulated activities or ancillary activities.*"

(iv) Provisions requiring professional persons to act with integrity or to be of sufficient repute may reach into private life only when conduct that is part of a person's private life realistically touches on their practice of the profession concerned. The conduct must be qualitatively relevant because it engages the standard of behaviour set out in the regulatory code concerned; and

(v) In considering that question, the decision-maker should consider whether public confidence in the profession would be harmed if the public, assumed to have knowledge of the facts, found that a person who behaved in a manner under scrutiny was able to continue to practice his profession.

The decision of whether to withdraw approval should begin with the FCA's statutory objectives, the relevant objectives in this case being the consumer protection objective and the integrity objective. When considering the relevance of behaviour that takes place in a person's private life, the key issue is whether the behaviour concerned realistically engages the question as to whether the individual poses a risk to (i) consumers and (ii) to confidence in the financial system.

## The Decision

The Tribunal found the FCA's arguments linking Mr Frensham's conviction to the consumer protection objective to be speculative and unconvincing. There was no evidence Mr Frensham had abused the trust he had in relation to his clients in the four years since his conviction. In fact, the FCA's approach to allow Mr Frensham to carry on in business undermined their concerns that he would not act with integrity in relation to his dealings with clients. The Tribunal also accepted, as in *Beckwith*, the qualitative relevance of Mr Frensham's conduct to his role as a financial advisor had not been demonstrated.

The FCA also sought to link Mr Frensham's conviction to the integrity objective – and the possible loss in public confidence in the industry if a person convicted of an offence of this type was allowed to continue to work as a financial adviser. Here the Tribunal found the FCA's argument more convincing (applying *SRA v Main [2008] EWHC 3666 (Admin)*). Mr Frensham's reputation was clearly damaged, but the relevant question was whether the offence affected his reputation as a financial advisor. Although a considerable number of clients left following the conviction, most stayed with him knowing of his conviction. Here again, the Tribunal was critical of the FCA's failure to provide evidence linking the offence with the detriment to public confidence.

Ultimately, however, the Tribunal held that the FCA was entitled to make a prohibition order. It was held that the circumstances in which Mr Frensham's offence came to be committed, in tandem with his (i) breach of bail conditions; (ii) failure to be open and transparent with the Authority in communicating material facts about the conduct referred to above (including being struck off by the CII); and (iii) lack of remorse or acceptance that he had committed an offence meant that he lacked integrity.

In particular, the Tribunal found that Mr Frensham had prioritised his own interests (and those of his firm) above the need to comply with his obligations. The Tribunal emphasised the importance of issues being put on the "table" with the FCA and entering into a dialogue around matters going to fitness. A person of integrity "*would not seek to keep such matters back from the Authority but would recognise that it is much better if one is up front with difficulties*".

The Tribunal judgment is peppered with critical observations of both the way the FCA approached the regulatory decision-making process and its failure to provide appropriate evidence to support its case against Mr Frensham. However, the Tribunal provided an implicit warning to applicants that seeking to exploit procedural deficiencies is unlikely to prove to their advantage, even where the deficiencies may have led to unfairness. Since the Tribunal was hearing the case afresh and without deference to the FCA's original decision, the FCA was entitled to substantially amend its case and rely on additional facts and evidence not relied on in the regulatory proceedings.

## C&G Analysis

- The judgment contains essential guidance for firms considering how to approach allegations both under the COCON and the SMCR regimes. The FCA has made it clear that "*non-financial misconduct is misconduct, plain and simple*"[2] and that it falls within the scope of the FCA's regulatory framework. A firm is permitted (and will be expected) to scrutinise conduct that took place in a person's private life where relevant to their role.

- Given the Tribunal's focus on the regulated person putting relevant regulatory matters "*on the table*" as part of a continuously proactive relationship, firms will be expected to provide information to allow the FCA to make properly informed and objective decisions concerning a person's conduct. Firms should demand the same transparency from its staff (and inform employees of the type of incidents in their private life that are notifiable). Deciding whether to notify the FCA of non-financial misconduct is not straightforward but there would need to be an assessment of the connection between the misconduct and the regulated function of the individual. The mantra for all concerned must be, if in doubt, disclose.

- Following the Court of Appeal's judgment in *Beckwith*, the Tribunal pushed back on dogmatic regulatory conclusions that public disgrace and improper conduct (absent dishonesty) carried out in a person's private life must make the person unfit to carry out their designated function. Importantly the conduct must be qualitatively relevant to their regulated role. This assessment will involve a careful analysis of how the conduct alleged could be said to impact their professional role and personal integrity.

- Integrity should be assessed objectively by the ethical standards expected of the professional and whether public confidence in the firm would be harmed should the person be allowed to continue to practice. This is a difficult assessment to make but we suggest a valuable yardstick would be how the firm's clients or stakeholders would react if they had knowledge of the facts. On the basis of the clients who continued to work with Mr Frensham (and absent specific evidence provided by the FCA), the Tribunal did not consider that his conduct sufficiently harmed public confidence to justify a prohibition order on its own.

- Ultimately, a person's integrity will be assessed by how they deal with the consequences that follow from the misconduct as much as the misconduct itself.

[2] Christopher Wollard, former interim CEO of FCA, from a speech in December 2018.

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