

DP21/2: Diversity & Inclusion in the financial sector - working together to drive change

BSA Response

Restricted
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Summary

The BSA and its members strongly support the steps being taken by the Bank of England, PRA and FCA to engage in a more formal dialogue on diversity and inclusion.

We very much welcome the opportunity to contribute to the regulators' developing views and policy on these important areas. As the dialogue progresses we encourage the regulators to continue a programme of proactive engagement to ensure that their Consultation Paper next year takes account of as wide a range of views as possible. We want to proactively engage with the regulators and to actively support progressing diversity and inclusion across our sector.

We respond to the questions in DP21/2 later in this response, and our key points are as follows:

1. **Driving Change:** The regulators should consider how their proposals would ultimately fit into wider government and social initiatives to encourage and achieve greater diversity and inclusion. We think it is absolutely right to consider how best to reshape the financial services sector into a more diverse and inclusive one. However, that ultimate goal cannot, we believe, be realistically achieved solely through the commendable actions and vision of the regulators or the regulated. Forcing change may ultimately lead to poor outcomes for firms and consumers alike. Change is already taking place in wider communities, which should naturally lead to changes in the industry (supported, of course, by the approach and strategies of individual firms). There needs to be a clear link to other government and societal initiatives, and without this there is a risk of failure. We already know of certain roles within the sector which are (a) hard to recruit to for smaller firms, and (b) dominated by people with certain characteristics. There will need to be a real effort, not just from FS firms, but from educators and the government to encourage people with more diverse characteristics into the industry.
2. **Diversity of Thought:** We agree with this concept and how it is presented in the DP. In establishing cognitive diversity it is important to consider not just individual "thinking styles", but also people's background and life experience. Measuring that, and how firms factor this into recruitment and performance management could be challenging and (as with all of this) the more advice, guidance and sharing of good practice that can be achieved, the better. In order to achieve diversity of thought, the regulators themselves should consider their own expectations for Board and senior management appointments.
3. **Accountability:** Board accountability for promoting diversity and inclusion will be critical to successfully achieving a more diverse and inclusive sector. We do have some concerns around the FCA's ability to withhold regulatory approval for certain roles on the grounds of diversity and inclusion – could the regulators themselves fall foul of other legislation such as the Equality Act 2010 were they to do so? Any proposals of this nature will require thorough consideration in the context of the wider legislative environment.

4. **Proportionality:** Throughout the DP, the regulators talk about proportionality, and this is an area of particular interest to us and our members. The PRA is already advocating a “strong and simple” approach to the regulation of smaller financial services firms and taking a proportionate approach here, without diluting the intent, will be welcomed. Of course, proportionality in the context of diversity and inclusion should not just be focussed on the scale of a firm. Many larger firms will have established and stable populations of senior managers, and where that is the case, a proportionate approach to expectations of those firms in relation to pace of change at the very least will be essential. We are concerned that the regulators ensure that whatever is ultimately proposed does not cut across other regulatory requirements, such as the application of the Common Bond in the case of Credit Unions, which may have been established to service particular groups of people.

5. **Data:** We understand that there is a need for data both from the point of view of understanding where firms are now, and being able to set targets and measure progress. Quantitative data is only one side of the equation, however, and qualitative data is perhaps even more important to understanding real progress in increasing diversity and inclusion in the sector. For example, movement of staff in smaller firms will have a disproportionate impact on statistics measured by percentage alone. Care needs to be taken in relation to the potential increased administrative burden of collecting data and also not to fall foul of, or place firms in a position where they may fall foul of, other legislative requirements, particularly as regards sensitive data or the risk of identifying individuals.

Response to Questions

Q1: What are your views on the terms we have used, how we have defined them, and whether they are sufficiently broad and useful, now and in the future?

We are supportive of the proposed approach of concentrating on diversity of thought, and the factors that have been identified as leading to diverse thinking appear appropriate. The DP rightly identifies that some characteristics are visible and measurable, while others such as sexual orientation may not be. Care needs to be taken in how firms arrive at what they think evidences diversity of thought. It has the potential to be used as a means to avoid talking about/addressing demographic diversity, as an example. For instance, just because one person likes boats and another likes bikes doesn't necessarily evidence diversity of thought.

It makes sense to us to consider diversity of thought in line with the 9 protected characteristics as well as socio-economic factors, gender and cultural background, and some of our members have suggested that this is one area in which guidance from the regulators would ultimately be useful in helping firms assess what might evidence diversity of thought in relation to each. Please see our comments later in this response regarding ability to collect certain of this data.

We entirely agree that inclusion is integral to creating a more diverse financial services sector, and the proposed definition is in our view workable. Bringing in reference to psychological safety, ability to speak freely without fear, feeling empowered to challenge, raise concerns and perform to one's best are important aspects of this.

The DP says that inclusion can be defined as “the practice or policy of providing equal access to opportunities and resources for people who might otherwise be excluded or marginalised – eg due to demographic characteristics”. We would suggest that rather than “might otherwise **be**”, this should instead refer to “might otherwise **feel**”, which would better reflect that people need to *feel* as well as *be* included.

Q2: Are there any terms in the FCA handbook, PRA Rulebook or Supervisory Statements or other regulatory policies (for any type of firm) that could be made more inclusive?

While the regulators have already made attempts to use more inclusive language in rules and guidance, including removal of words such as “chairman” and references to “Chinese walls”, more could be done to achieve this. A review of all material issued by the regulators to ensure that it is universally using inclusive language would be helpful. This should include the replacement of the following terms *throughout* their materials:

- ✚ Replacing any reference to “women” and “men” with “people”
- ✚ Replacing “her” or “his” with “their”
- ✚ Replacing “blind spots” with “not previously considered or aware of”

For example, a rudimentary search of the FCA Handbook for the words “he should” throws up a number of instances where this potentially exclusive language is used (MCOB 5.9 being one example). However, care should be taken in doing this to ensure that it does not lead to a lack of clarity over the meaning of terms (thinking back to proposals in the recent past to use an alternative to the word “grandfathering”).

We have also encountered instances of non-inclusive gender-specific language (such as the phrase “key man” - <https://www.fca.org.uk/firms/review-resources>) being used in scenarios where this is not necessary.

We would also encourage the regulators to refer to “addressing underrepresentation” rather than “increasing diversity” in order to ensure that non-diverse groups are not labelled as a problem that needs to be solved.

Q3: Do you agree that collecting and monitoring of diversity and inclusion data will help drive improvements in diversity and inclusion in the sector? What particular benefits or drawbacks do you see?

We entirely agree that “good” data is critical to understanding the current position, monitoring progress, identifying barriers to it and selecting the most effective interventions. We also agree that collecting and monitoring data relating to diversity and inclusion has the potential to drive improvement.

In order for this to be achieved, however, there are two key factors:

1. The data needs to be complete. Where it is not, it will be important to ensure that firms and the regulators take sufficient account of qualitative and other data evidencing how diverse and inclusive firms are. For example, many firms make use of staff surveys, which can help inform, although these are clearly not without flaws, especially where there are under-represented groups.
2. There needs to be a culture of trust and transparency to ensure that colleagues know why firms are asking for information, and what is being done with it to drive fair outcomes. Feedback from our members suggests that without that, collection of this information may cause concern amongst overrepresented groups, who think that it means that they will not progress in their career when compared to other colleagues.

This means that strong and supportive leadership will also be required to help colleagues understand the importance of their data and fostering a clear understanding of its purpose and how it will be used.

Benefits could include:

- Tangible evidence of progress (or otherwise)
- Greater knowledge of gaps, allowing action to be taken to address them
- Easier for firms to set targets and evidence progress towards them
- Over time, collecting and publishing data becomes normalised and acceptable
- Brings greater focus on diversity and inclusion as part of firms' approach to both recruitment and customer engagement

Drawbacks could include:

- Over-reliance on quantitative (and perhaps incomplete) data
- Inaccurate/incomplete data leads to firms/regulators focussing attention in the wrong areas
- Firms are unable to establish a true starting point, due to lack of data
- Firms that are less able to provide data (whether due to size or other issues) being unfairly considered less diverse and less inclusive
- Legacy systems unable to cope with collection of data

It is also worth remembering that for some firms there will be a lot more work to do to begin collecting and measuring data.

Q4: Do you have a view on whether we should collect data across the protected characteristics and socio-economic background, or a sub-set?

We think that in an ideal world, you would seek to collect all of the data specified, although collection of socio-economic data is perhaps more problematic. As stated above, however, some data may be easier than others to collect. For example, during September 2021 we surveyed our membership on a number of D&I-related matters linked to the DP, and over 50% of our 19 respondents (representing 40% of our membership) indicated that they would find it difficult or very difficult currently to collect data on all of the protected characteristics. However, 80% said they expected to be able to collect more over the next 12 months. In terms of socio-economic data circa 80% said they would find it difficult or very difficult to collect this data.

With that in mind, the regulators should consider whether monitoring may be better focussed on the firm's own policies, how it is evidencing progress against them and any targets it has set as part of that policy or elsewhere. There is a risk that in generalising, the regulators could lose sight of whether or not the firm has in fact truly achieved the desired levels of diversity.

That said, there could be a core set of data drawn from that specified, with others being gathered on a best endeavours basis. Given that an individual's willingness to share data relating to protected characteristics can be influenced not just by the workplace, but by other social and cultural factors, we do not consider that firms should be viewed negatively or adversely impacted if they are unable to obtain data of this nature. That would, of course, be provided that they are able to evidence the actions they are taking to improve diversity and inclusion in other ways.

Our members have indicated that there is scope for socio-economic data to be distorted, for example there is evidence that:

- People's parents will have had such a broad range of jobs, that don't always neatly align to predefined list
- People who went to private school are known to select "yes" to "free school meals"

- If you grew up outside the UK, socio-economic questions are typically more difficult to answer

Given that, it may be better to require firms to track socio-economics for current and future board appointments to identify whether there is a “mould” that needs to be more flexible. This would be aided by removing specifics for education and/or types of institution when hiring and focussing instead on achievement and impact. Firms could also be offered more encouragement to invest in underinvested communities to influence life outcomes such as financial education, access to apprenticeships etc.

Further, some of our members have found collecting meaningful employee data for diversity a challenge. They have found that despite creating what firms believe to be a safe environment, colleagues can still be reluctant to voluntarily share personal information. That in itself leads to the challenge that without enough information, understanding whether action is needed becomes more difficult. In turn, this leads to the conclusion that if collection of information in relation to protected and other characteristics becomes mandatory, then consideration should be given as to whether a change in data and privacy is necessary.

Our members have also indicated that they consider diversity more widely than in relation to just the protected characteristics plus socio-economic factors. Other factors that they reference include whether people are carers, veterans and the impact of the menopause.

Q5: What data could the regulators monitor to understand whether increased diversity and inclusion is supporting better decision making within firms and the development of products and services that better meet customers’ needs?

Clearly, the data that the regulators are proposing to collect will not be effective in isolation in indicating whether increased diversity and inclusion is supporting:

- ✚ Better decision making, and
- ✚ Development of products and services that better meet customers’ needs.

Other types of data that could foreseeably be of some use in evidencing that include:

- ✚ Board Minutes evidencing challenge and in particular challenge to “group think”
- ✚ Whistleblowing data – arguably, if there is a more inclusive culture in the firm, people will feel more comfortable speaking up and over time there may be less formal internal/external whistleblowing incidences
- ✚ Complaints data around the suitability of products
- ✚ Employee diversity at every level - individual contributor, first line manager, manager of managers, Executive Leadership Team and Board
- ✚ Employee Inclusion – firms could disaggregate engagement survey data to assess whether underrepresented groups are having an equally good experience as overrepresented groups. Specific focus could be given to being involved, valued and heard
- ✚ Customer diversity being measured across all product research, member panels and other member engagement forums
- ✚ Customer inclusion – firms could disaggregate Net Promoter Scores to assess whether underrepresented groups are having as good an experience as overrepresented groups

In the BSA’s September 2021 survey, we asked members about the data already collected by them and how that is currently monitored. As stated above, circa 40% of our 49 members responded to that survey. Of those firms, 80% monitored diversity in some way – gender pay gap, targets and performance objectives, regular engagement surveys, numbers of

bullying/harassment claims. Around 90% considered themselves to be monitoring inclusion through mechanisms such as recruitment, employee surveys, product design and membership of projects and internal working groups.

Q6: What are your views on our suggestions to approach scope and proportionality?

We are pleased to see that the regulators acknowledge that a one size fits all approach is inappropriate, and that it is essential to encourage diversity and inclusion in a way that is appropriate to a firm's size and complexity. We are also pleased to note that there is an intention to avoid introducing rules that would not be effective or appropriate for smaller firms. That said, work required to drive change may in practice be easier in smaller (if not the smallest) firms, as implementing such change in larger organisations, especially those with long histories, could be more of a challenge.

We agree that small firms, with few employees, could not meaningfully enact many elements of the options being proposed. It will be helpful that the regulators are considering including them only in a very limited way and can see the benefit of keeping requirements at a high level such as requiring them to respond to the needs of their customer and potential customers with respect to the products and services they deliver and not engaging in unlawful discriminatory practices. Clarity on what will and will not be expected will be necessary.

Q7: What factors should regulators take into account when assessing how to develop a proportionate approach?

The intention of applying options in the paper only to large firms is a useful starting position. We would encourage the regulators, however, to take care in applying a proportionate approach, and not to base this solely on size. For example, it might be tempting to apply certain targets/impose certain data requirements on larger firms. That might not be appropriate, however, compatible with existing employment legislation or possible in practice in a defined timeframe where (for example) firms have very stable senior management teams.

Proportionality could also be applied to the timeframe within which firms might be expected to deliver evident change. In these (and potentially other) circumstances, proportionality could perhaps be linked to the firm's own Diversity and Inclusion policy, rather than the regulators' policy/expectations by which it seeks to see change in firms over or under a particular scale.

In adopting a proportionate approach, particularly to data collection, consideration should be given to whether or not incomplete/inaccurate data may mask an issue or indicate that there is one, when that might not be the case.

We like the concept of basing proportionality on business volume, along the lines of those adopted for the application of the SM&CR. In doing so, however, we would urge clarity on requirements and timescales for firms moving from one category to another.

Our members have suggested that it may also prove appropriate to consider "regionality" in application of proportionality. For example, consider whether a firm's ambition should reflect the demographics of where it physically employs people in the case of employee diversity, or where customers of a firm live in the case of customer diversity.

Q8: Are there specific considerations that regulators should take into account for specific categories of firms?

The DP itself points out the difficulties that some smaller firms may face in collecting suitably anonymised data, and this needs to be carefully considered as part of the next stage of the regulators' thinking.

The impact on mutuals of any proposals to define size using definitions based on those contained in the Companies Act should be carefully considered. Perhaps more complex is the need to recognise that the very purpose of some firms, credit unions being one example, is to serve people with certain characteristics. For credit unions, the application of the common bond will also need to be carefully considered when assessing diversity and inclusion in that part of the sector.

Q9: What are your views on the best approach to achieve diversity at Board level?

There is no question that the best approach to achieving diversity at Board level is for the Board itself to embrace diversity and inclusion, set a clear strategy, monitor its delivery and take action to address any barriers. Increasing awareness of Board members and those members then holding themselves to account will be critical.

To support that a recruitment/Board Succession strategy that properly takes account of diversity and inclusion, and which could be mandated by the Board as part of its overall strategy for diversity and inclusion could be helpful.

Targets and measures can also drive change. As the DP points out, some larger firms are already mandated to achieve a target for the under-represented gender at Board level. This could, of course, be more difficult to achieve for smaller firms and so the regulators should consider how they/smaller firms could evidence diversity of thought and demonstrate that they are driving forward an inclusive culture. This could be based on qualitative metrics such as staff surveys, the use of inclusive language in internal and customer facing engagement etc.

Q10: What are your views on mandating areas of responsibility for diversity and inclusion at Board level?

We consider that this is appropriate and that in order to achieve real change, areas of responsibility should be mandated at Board level. The DP suggests, and we agree, that:

- ✚ The Board should hold management to account for promoting diversity and an inclusive culture that fosters open exchanges of ideas, constructive debate and sound decision-making.
- ✚ The Board should set the diversity and inclusion strategy and oversee its progress.

Consideration should also be given to whether firms themselves, or even the regulators, might mandate requirements around aspects such as succession planning, shadowing and sponsoring, trainee board members and achieving a mix of socio-economic backgrounds and skills.

However, the regulators should also bear in mind that certain firms may face issues where requirements are mandated. For example, a credit union whose membership comprises only police officers, may face issues with the application of the Common Bond. This would need to be carefully considered and addressed as part of the next stage of the consultation.

Q11: What are your views on the options explored regarding Senior Management accountability for diversity and inclusion?

We agree with the concept of Senior Management having accountability for diversity and inclusion. Linking this to the existing accountabilities in relation to culture would appear to be a good approach.

Q12: What are your views on linking remuneration to diversity and inclusion metrics as part of non-financial performance assessment? Do you think this could be an effective way of driving progress?

We understand the rationale for this concept, but have some reservations as to how workable this would be in practice, especially for those firms that may find it difficult to obtain meaningful data. We would also caution about potentially linking this only to quantitative measures. As we have pointed out previously, for many firms, qualitative data may be equally if not more useful in assessing how diverse and inclusive they are. That said, the proposed approach of not being prescriptive and instead focussing on sharing good practice at individual and firm level would seem to be a good starting point.

The regulators' intent to potentially prescribe that firms' remuneration policies should ensure that all types of remuneration do not give rise to discriminatory practices is interesting. We agree with that as, without caution, there is a risk that firms could fall foul of existing legislation. While its intent is admirable, in practice, were policies and (perhaps more importantly) practices to result in discrimination, there would be recourse under existing legislation such as the Equality Act 2010. Any move to prescribe this would need to be carefully constructed so as not to be at odds with existing legislation designed to ensure that this does not happen.

With the business and moral case for diversity becoming overwhelmingly compelling in wider society, it is hard to justify why executives need financial incentives/disincentives to motivate them to do the right thing. Surely the emphasis for firms should be on building an environment where increasing diversity is not an afterthought or a responsibility outsourced—it must be an essential element of their job for which they receive their base salary.

Q13: What are your views about whether all firms should have and publish a diversity and inclusion policy?

We agree this should happen, and that it is important for colleagues and customers to know what to expect from firms that they work for or do business with. In our September 2021 survey of members, 85% also agreed.

Q14: Which elements of these types of policy, if any, should be mandatory?

We think it could be difficult to mandate what should be included in the policy as what may fit one firm may not fit another. As a minimum, we would expect to see clear identification of the purpose of the policy and commitments made by the firm to further diversity and inclusion. We consider that the policy itself should be high level with the Board holding senior management to account for delivery of any targets identified in the policy. Some of our members have suggested that publication of a firm's stance on bullying, harassment, racism, homophobia and the like, as well as the action that could be taken should any of those occur may be helpful and could contribute to reinforcing a firm's culture of inclusion.

The consensus amongst our members, based on our September 2021 survey, was that clear objectives, realistic goals and how these will be measured and reported should form part of a firm's policy.

Q15: What are your views about the effectiveness and practicability of targets for employees who are not members of the Board?

In our view this is directly influenced by the size and complexity of the firm in question and (in part) it's geographical location, its customer base and the location of that.

For smaller firms it may not be practical, for example, to impose targets beyond the level of management immediately below the Board, and even that may be taxing for the smallest of firms. Some of our members have also pointed out that doing so may risk alienating some groups when recruiting. Proportionality will again be critical to make sure that unrealistic and unachievable targets are not being imposed. More widely, however, there ought to be nothing to stop firms from making sure that leaders in every team and at every level know what is expected, how it will be measured and how the firm will support them in making their own changes, building confidence and measuring their own progress.

Q16: What are your views on regulatory requirements or expectations on targets for senior management population and other employees? Should these targets focus on a minimum set of diversity characteristics?

The response to this question is influenced by the type of targets that firms would be expected to set. A blunt approach to setting targets would not be effective in our view, especially where intersectionality is at play, nor would it take account of diversity of thought, which might be being very well accounted for.

If targets are to be based purely on characteristics that are immediately apparent, gender and ethnicity perhaps being the most obvious of these, then we do not consider that that is appropriate, given the number and nature of characteristics that are not so easy to measure.

There is a danger that focussing on setting targets for a subset of the characteristics results in them being perceived as being more important than others.

Rather than the regulators setting targets, a better approach might be for them to mandate firms to set targets, and then monitor their progress against them. Should that not be effective in increasing diversity and inclusion over a defined period of time, then that might be the point at which the regulators step in and impose targets at individual firm level. Taking this approach might also allow the regulators and firms to have more complete data on what data/targets are achievable and measurable. Overall, we think that there needs to be a recognition that there is unlikely to be a quick fix. Given that, consideration should be given to whether firms should establish a roadmap (perhaps as part of their overall strategy for diversity and inclusion) rather than just set targets.

We believe that there may be some merit in setting targets for others, such as customer facing roles. As the DP points out, this could help in understanding and serving diverse customers. As pointed out above, however, some of this will depend on the region in which the firm/branch is located and its demographics, and we question whether or not setting targets of this type should be the role of the regulators. In order to truly influence and ensure good outcomes for diverse customers/potential customers, there may also be merit in setting targets for central functions such as marketing and product development teams. Again, though, we think that that should be for the firms to determine based on target market and strategy rather than being mandated by the regulators.

Q17: What kinds of training do you think would be effective in promoting diverse workforces and inclusive cultures?

We agree that an element of training will be essential on areas such as the use of inclusive language, both in conversation and written communication both internally and with 3rd parties (including customers). We do not have a strong view on what training would best promote diverse workplaces and inclusive cultures. In practice, we would expect training requirements to be assessed based on how advanced a particular firm is in having a diverse workforce and inclusive culture. Training on how to consciously include every day, and building this in to

decision making when hiring, promoting, giving recognition and forming project teams could be helpful.

Feedback from the BSA's Diversity and Inclusion Working Group is that sharing of best practice and experience can be beneficial in helping firms understand what they can do to become more diverse and inclusive. Perhaps the regulators could consider whether they might be able to provide a hub for sharing of such ideas and practice.

Q18: What kinds of training do you think would be effective for helping understanding of the diverse needs of customers?

Our members have suggested that understanding the ever-changing population, what happens when diversity and inclusion is missing, and how to ask the following questions every time products and services are reviewed would help:

- “Who aren't we serving?”
- “Are we ok with that? If not, what will we do?”

Q19: What are your views about developing expectations on product governance that specifically take into account consumers' protected characteristics, or other diversity characteristics?

We consider that it would be hard to develop a one size fits all approach to this, especially if there is (as the DP suggests) a different and proportionate approach taken to firms based on criteria including size.

Q20: What are your views on whether information disclosures are likely to deliver impact without imposing unnecessary burdens? Which information would deliver the biggest impact?

We agree that collecting information should be considered an investment rather than a burden, although there is less value in patchy data. However, considering whether its collection would impose an unnecessary burden brings a host of factors into play, including:

- how easy it is for firms to collect the data ultimately landed on as being required,
- whether legacy systems can cope with it, and
- how willing employees are to share it.

If the data is good and complete, and consistently so amongst the firms providing it, then we agree that it *could* have a positive impact. That said, it is questionable whether the reporting of gender pay gap data has made a difference, so measuring that impact will be important.

In terms of biggest impact, there are obvious factors such as gender and ethnicity, which one might be tempted to focus on. However, as mentioned elsewhere in this response, in order to create a complete picture at firm as well as sector and industry levels, consideration needs to be given to how qualitative data is accounted for.

Q21: How should our approach for information disclosure be adapted so that we can place a proportionate burden on firms?

There should be a clear criteria established which, if met, requires full or partial disclosure of whatever data it is ultimately concluded that firms should collect. We agree that a standard

reporting form seems appropriate, although whether or not that fits with a proportionate approach in practice would depend on its construct, nature of the information being sought and provided etc. Firms must be given an adequate lead-in time for collection and submission to allow systems and practices to change in line with what's required.

Q22: What should we expect firms to disclose and what should we disclose ourselves from the data that we collect?

Subject to all of our other comments in this response, we think that there is merit in an aggregated disclosure report. At the very least, this should demonstrate progress across the industry. It may also be useful if the regulators collected the data in such a way as to allow it to be broken down further – insurance, banking etc.

Whatever approach the regulators decide to take to data collection, it would be helpful to ensure that firms are given plenty of advance notice as to what will be required, and for the regulators to ensure that how this is collated and presented could be dovetailed with information being collected in other sectors. This could allow the data to input into the creation of an overall UK-wide picture.

Particularly for smaller firms, real care will need to be taken both by the firm and by the FCA were it to publish aggregate data especially if there was a risk that individuals could be identified from that. We have concerns over the potential administrative burden and advice requirements that could be placed on firms who have concerns over falling foul of GDPR requirements in collecting and sharing data of the types contemplated.

In general terms, and subject to the above, aggregated data on firms' position on defined characteristics relating to senior management as distinct from, or in addition to all employees would seem to be a good starting point, as would the publication of firms' Diversity & Inclusion policies. How would the regulators suggest that diversity of thought should be measured and reported on?

We have some concerns regarding the potential for adverse impact on firms that, for whatever reason, were unable (or not required) to publish data that others are. It seems to us that there could be a risk of market distortion, competition being affected and customers choosing not to use firms if this information is not available. There may be a communication/education role for the regulators as well as firms in order to mitigate that risk, and perhaps consideration should be given to controls or restrictions around how firms report/publicise more widely that they are collecting information on diversity and inclusion.

Q23: What are your views on how we should achieve effective auditing of diversity and inclusion?

Extending the work already undertaken by audit teams in relation to culture and risk would seem to be the most straightforward way of achieving this, although not without its challenges in terms of competence and training of audit personnel. Including a diversity and inclusion audit as part of the FCA's culture audit seems appropriate, although a balanced approach should be taken to assessment of where a firm is in relation to diversity and inclusion. Apart from anything else, and especially where there is incomplete data, this is likely to be difficult to measure. Further, a standard approach to audit across all firms would not be effective, particularly in measuring inclusion – qualitative rather than quantitative measures again become important here.

Q24: How can internal audit best assist firms to measure and monitor diversity and inclusion?

See response to Q23. In addition, members have suggested that the following activities might support internal audit in any measuring and monitoring:

- 🚧 Completion and comparison of diversity information year on year
- 🚧 Accurate recording of initiatives in place to address underrepresentation
- 🚧 Evaluation by firms of which initiatives are driving most change
- 🚧 Reporting of progress against the firm's D&I policy/strategy

Q25: Do you agree that non-financial misconduct should be embedded into fitness and propriety assessments to support an inclusive culture across the sector?

Yes, and we are encouraged by some of the action already taken by the regulators where there have been instances of non-financial misconduct at an individual level. If this is pursued, guidance would be essential, although we have concerns about potential future litigation risks for both firms and potentially also the regulators, depending on how that guidance is framed. Care would need to be taken to avoid unnecessary increased risk of employment-related claims or tribunals.

Q26: What are your views on the regulators further considering how a firm's proposed appointment would contribute to diversity in a way that supports the collective suitability of the Board and senior management?

We understand the FCA's rationale for increased scrutiny of firms' senior management (for firms subject to SM&CR). We can, however, foresee a number of practical issues associated with collection of diversity data as part of the information collected for SMF applications. Remember that this information will often be obtained before the applicant has any relationship of employer/employee with the firm, which may make them more reticent to provide certain information. Depending on who and how the data is collected, there is a potential increased risk of allegations of discrimination against both firms and the regulators. Should such an approach be taken, that risk would need to be fully understood and appropriately mitigated for the protection of all parties.

Q27: What are your views on providing guidance on how diversity and inclusion relates to the Threshold Conditions?

We think that exploring how this diversity and inclusion relates to the Threshold Conditions would be helpful. If fitness and propriety is impacted at individual level, then we see no reason why that should not also be the case at firm level. Subject, of course, to the other comments we have made in this response.

Q28: Do you have any suggestions on which aspects of our supervisory engagement with firms that you think could be improved to help deliver and support greater diversity and inclusion?

Collection of data coupled with more questions from supervisors on how firms are embedding D&I and how the firm is creating a culture of inclusion to unlock its benefits would be a good starting point. The use of deep dive assessments into individual firms' progress against their own Diversity and Inclusion Policy/Strategy may also be useful. A requirement on firms to present an annual report on their position on diversity and inclusion vs strategy to the Board might also enhance visibility, although a proportionate approach would need to be adopted to any such reporting requirement.

Some firms have more direct dialogue with supervisors than others and, particularly if diversity and inclusion is to be linked to something as fundamental as the threshold conditions, there may need to be more frequent supervisory engagement. The regulators would need to ensure that it was appropriately resourced in terms of numbers and skills to support that.

The regulators have stated that in their supervision, they want to:

- ✚ Understand the role of leadership, how diverse workplaces can create a safe environment, what actions are being taken to address gaps and how the firm is assessing success
- ✚ See how D&I is embedded at all levels and how representative firms are of the people they serve
- ✚ Understand how firms are taking D&I into account in their strategies, products and services they design and the diverse needs of those they serve

While this is commendable, and might provide an opportunity for the regulators to blend ESG/D&I strategies across the sector, the question that arises is what the regulators' expectations of firms will be in evidencing all of this. We would urge pragmatism and a proportionate approach and that this is fully assessed in any cost benefit analysis.

Q29: What impact do you think the options outlined in this chapter, alongside the FCA's proposals for a new Consumer Duty, would have on consumer outcomes?

Of themselves, we believe these proposals have the potential to have a positive impact on consumer outcomes for all the reasons stated throughout the DP.

While we fully support the FCA's drive to ensure that firms focus on good consumer outcomes, getting it right first time and putting customers in a position where they can act and made decisions in their own interests, we disagree that the introduction of a new Consumer Duty is the way to achieve this. We think it is not helpful to link the positive impact that the regulators' proposals on diversity and inclusion could have to a consumer duty, when we do not believe that a new consumer duty would achieve the FCA's desired outcomes any better than the existing regulatory principles for all the reasons set out in our response to their consultation on the Consumer Duty.

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