

Strengthening accountability in banking

BSA response to FCA CP 16/27:
Conduct rules for standard/notified
NEDs

3 January 2017

 **Building Societies
Association**

Introduction

This BSA response supports the proposal in FCA CP16/27 that 'standard' - sometimes called 'notified' - non-executive directors (NEDs) should be subject to the regulators' individual conduct rules and to rule 4 of the senior conduct rules.

The FCA's proposal aligns with the position consistently taken by the BSA that it is inappropriate for only some of the members of a unitary board of directors to be subject to the relevant regulatory conduct rules.

It would also be very helpful if, once any teething problems and issues in the SM&CR rules have been remedied or clarified, the regulators would allow a prolonged period for the new regime to bed down, before proposing any more substantive changes. A degree of consistency, generally absent in relevant law and regulation for about two decades, would greatly help consumers, firms and the economy.

Questions and BSA responses

Q1: Do you agree with our proposal to apply the 5 FCA individual conduct rules and the senior conduct rule 4 to standard NEDs?

1. The BSA strongly supports the FCA's proposal. The BSA's long-term position has been that, in a unitary board, all directors should be subject to the relevant conduct rules. For example, in April 2015 in our response to FCA CP15/5, we stated –

“But there is a clear risk the dual status of NEDs could introduce behavioural differences at board level: some NEDs could feel a higher level of personal responsibility and risk than others. There is a possibility that this divide in behaviours could potentially undermine the collective decision-making responsibility of the board. In addition, it may become increasingly difficult, or disproportionately expensive, to attract NEDs to “non-standard” roles.

One way to address this concern, if only partially, is to require all - that is “standard” and “non-standard” - NEDs to observe the conduct rules. This would ensure board decisions were based on the same underpinning principles and culture.”

2. In view of the fact that the individual conduct rules will apply to most ‘junior’ staff from 7 March 2017, the inclusion of standard NEDs within scope of the rules would help engender a culture within firms that “we are all in it together” regarding good conduct and TCF. In our response to CP15/5, among other things, we made the following point –

“Under current proposals, junior staff would be fully, and individually, captured by the conduct rules, while a large cohort of directors [standard NEDs] would not be. How can it be sensible to bring junior staff into the net, while excluding certain directors? Junior staff did not sit on the boards of the firms that failed prudentially and/or in conduct terms – directors did.”

Q2: Do you agree that Senior Conduct rule 1, 2 and 3 should not apply to a standard NED unless, as well as being a standard NED, they also fall into one of the other categories of ‘senior conduct rules staff’ as defined in the Glossary?

3. We believe that the inclusion of standard NEDs within conduct rules scope is compatible with the duties of a NED, but it should not be perceived either as expanding, or changing, the nature of their oversight role or in any way pushing them towards executive responsibilities. As we stated in our response to CP15/5 -

“The BSA supports the helpful clarifications (in COCON 4) about the limitations on the expectations regarding NEDs. For example, it is absolutely right to acknowledge that NEDs do not individually manage a firm’s business in the same way as executive directors and that they are not expected to assume executive responsibilities. We also welcome the fact that these, and other helpful, clarifications are carried forward in the draft supervisory statement (in Appendix 2 – see question 9 below).”

4. This principle is consistent with the FCA's proposal that senior conduct rules 1 (control), 2 (compliance) and 3 (delegation) should not apply to standard NEDs. The underlying obligations in senior conduct rules 1-3 are consistent with executive responsibilities and, in albeit in a different - oversight - way, with some of the specifically delineated responsibilities of the chairman, chairs of relevant committees and the senior independent director. However, they are not really consistent with the roles and duties of a notified NED.

5. Senior conduct rule 4 (openness with regulators) is fundamentally different in nature and we agree with the FCA that it's application is entirely consistent with the oversight role of a NED, including a standard NED. Therefore, we support the FCA's proposal to apply the rule to standard NEDs (see question 1 above).

Q3: Do you agree with our proposal to amend Handbook guidance to Rule 2 to clarify that this rule includes a director's conduct (whether executive or non-executive) when acting as a member of the Board or other governing body or of its committees?

6. This seems to be a sensible clarification.

Q4: Do you agree that the guidance COCON 1 Annex 1 on the role and responsibilities of NEDs should also apply to insurance firms?

7. While this is not of direct relevance to our members, it seems to us that - as a matter of principle - the broad requirements and guidance should apply across all regulated firms. Naturally, we appreciate that there should be proportionality in relation to size and scale of firms irrespective of sector but, otherwise, the key expectations should be broadly consistent across all regulated businesses. Therefore, we support the proposal.

Q5: Do you have any comments on our proposals to amend column J of the conduct breach report (Form H) to allow us to recognise which conduct breaches have been made by standard NEDs in RAPs?

8. It follows naturally from the main proposal in this paper that the FCA should have to amend Form H in the way suggested. Therefore, we also support this proposal.

9. We note that the PRA will have different reporting requirements. While we understand the distinction in this case, it is very challenging for firms (especially smaller ones) to have to distinguish the many different requirements stemming from twin-peaks regulation. Therefore, as a broad matter of principle rather than a comment on question 5, we continue to urge both regulators to be as consistent with each other in their approaches to regulation as is reasonably practicable given their different objectives.

By Chris Lawrenson
Head of Legal Services
chris.lawrenson@bsa.org.uk
020 7520 5915

York House
23 Kingsway
London WC2B 6LU

020 7520 5900
@BSABuildingSocs
www.bsa.org.uk

BSA EU Transparency Register No: 9: 24933110421-64

www.bsa.org.uk

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