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The FCA's Approach to Non-Financial Misconduct

Latest Cases and Observations

Contextual Backdrop

The FCA has long since regarded non-financial misconduct as potentially relevant to the integrity and reputation elements of a regulated individual's fitness and propriety. While not formally defined, non-financial misconduct is generally regarded as encompassing activities such as non-financial indictable criminal offences, bullying, victimisation, harassment, discrimination and, broadly, any other non-financial-related conduct (whether in or out of the workplace) which calls into question a firm's or an employee's integrity or reputation.

In last year's *Frensham* case[1], the Upper Tribunal considered **how relevant a (non-dishonesty-based) criminal offence committed in one's personal life is to the perpetrator's regulatory "fitness and propriety"**. Drawing upon (and following) an analogous solicitor case, the Upper Tribunal in Frensham effectively reined in the FCA from too readily linking (i.e. considering as relevant) non-work-related misconduct to the perpetrator's regulatory fitness and propriety to perform a regulated function. In doing so, the Upper Tribunal set out the approach to be taken when determining the relevance of non-financial misconduct in a regulatory context.

The latest in a series of non-financial misconduct-related prohibitions imposed by the FCA – that of Mr Ashkan Zahedian[2] in November 2022 – raises some interesting questions. On the basis of the published Final Notice, it is difficult to understand how (or, indeed, even whether) the FCA followed and applied the approach laid down by the Upper Tribunal in *Frensham* to Mr Zahedian's case. As explained in the following pages, the divergent regulatory findings of these two cases, are somewhat difficult to reconcile.

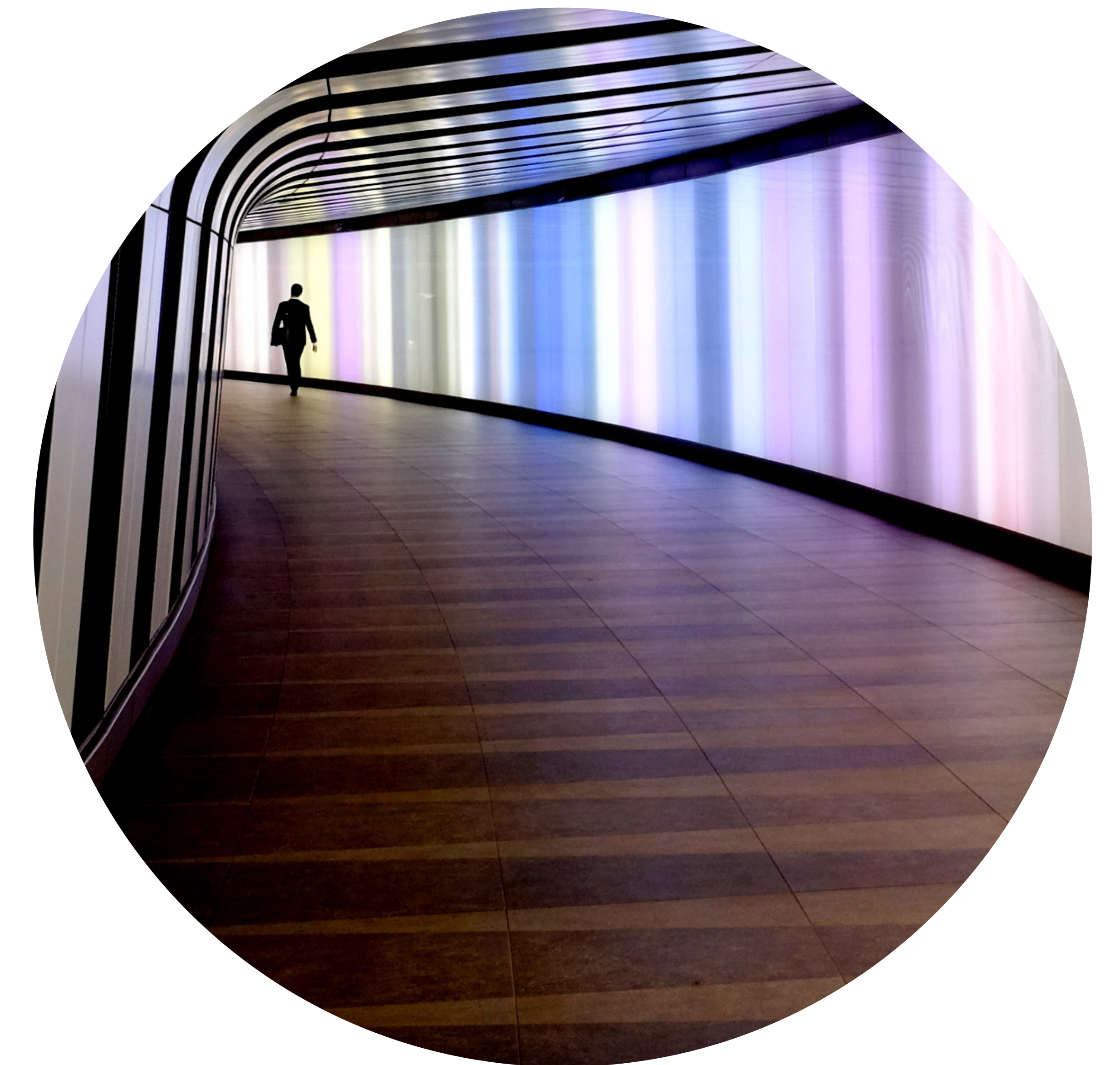
Case 1: Jon Frensham (2021)

In March 2017, Jon Frensham[3], an FCA-approved financial adviser, was convicted under section 1(1) of the Criminal Attempts Act 1981 for 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. Mr Frensham was sentenced to 22 months' imprisonment, suspended for 18 months.

In consequence, the FCA decided to withdraw Mr Frensham's regulatory approval and to make an order prohibiting him from performing any regulated function[4] – on the basis that, in light of his convictions, he was not a fit and proper person to perform any regulated function. Amongst other things, the FCA contended that the nature and circumstances of Mr Frensham's offending, including his seeking to exploit a child, showed that he lacked integrity. Additionally, the FCA argued that even though Mr Frensham's offence was not committed at work and did not involve financial dishonesty, it involved him deviating from legal and ethical standards – something which it considered was fundamentally incompatible with his role as a financial adviser. Further, the FCA cited a risk of erosion of public confidence if individuals who committed such misconduct and do not have the requisite reputation are permitted to continue working in the financial services industry.

Appeal

Mr Frensham appealed the FCA's determination to the Upper Tribunal. Mr Frensham contended that the FCA had wrongly applied the fitness and propriety test to the facts. In particular, he argued that the FCA had allowed irrelevant considerations to affect its judgement and did not have sufficient or any regard to relevant factors – for example, the fact that the conviction was not for an offence of dishonesty and that the offence was not related to his regulated activities.



Frensham was the first time that the Upper Tribunal had had to consider a case where the FCA was seeking a prohibition order against an individual based on that person's conviction for a criminal offence not involving dishonesty in circumstances where the behaviour concerned was unrelated to the individual's regulated activity.

Executive summary of the Upper Tribunal's findings

In summary (and significantly), the Upper Tribunal found that, had it been asked to consider the case on the basis of Mr Frensham's conviction *alone*, then it would likely have asked the FCA to reconsider its decision. The Upper Tribunal did, however, ultimately uphold the FCA's decision – but on account of two other factors, namely, Mr Frensham's breach of bail conditions and his failure to be open and transparent with the FCA[5].

Relevant rules and guidance

We summarise below the pertinent FCA Handbook provisions.

FIT 2.1.1G provides that {our emphasis}:

"In determining a person's honesty, integrity and reputation, the FCA will have regard to all relevant matters including, but not limited to, those set out in FIT 2.1.3 G which may have arisen either in the United Kingdom or elsewhere. The FCA should be informed of these matters (see SUP 10A.14.17 R and SUP 10C.14.18R), ***but will consider the circumstances only where relevant to the requirements and standards of the regulatory system****. For example, under FIT 2.1.3 G(1), conviction for a criminal offence will not automatically mean an application will be rejected. The FCA treats each candidate's application on a case-by-case basis, taking into account the seriousness of, and circumstances surrounding, the offence, the explanation offered by the convicted person, the relevance of the offence to the proposed role, the passage of time since the offence was committed and evidence of the individual's rehabilitation."*

EG 9.1 states that the FCA may exercise its power (to withdraw approval and impose a prohibition order) where it considers that it is appropriate in order to achieve its regulatory objectives.

When deciding whether to make a prohibition order against an approved person, the FCA will consider all relevant circumstances, including (amongst others): the relevance and materiality of the matters indicating unfitness; and the severity of the risk which the individual poses to consumers and to confidence in the financial system[6].

Mr Frensham appealed the FCA's determination to the Upper Tribunal. Mr Frensham contended that the FCA had wrongly applied the fitness and propriety test to the facts. In particular, he argued that the FCA had allowed irrelevant considerations to affect its judgement and did not have sufficient or any regard to relevant factors – for example, the fact that the conviction was not for an offence of dishonesty and that the offence was not related to his regulated activities.

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Upper Tribunal's observations and approach in *Frensham*

Having considered relevant legal authorities, the Upper Tribunal made some general observations, including (amongst others):

a. A regulatory obligation to act with integrity does not require professional people to be paragons of virtue;

b. 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

c. 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.

According to the Upper Tribunal, the starting point must therefore be the FCA's statutory objectives – namely, securing an appropriate degree of protection for consumers (the "consumer protection objective") and protecting and enhancing the integrity of the UK financial system (the "integrity objective"):

"… in deciding whether to make a prohibition order ***a key consideration is the severity of the risk which the individual poses to consumers and to confidence in the financial system, thus providing a direct link to the [FCA's] statutory objectives.*** *Therefore, in our view, 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 consumers and to confidence in the financial system."* {our emphasis}

Why did the Upper Tribunal not consider that Mr Frensham's conviction alone warranted a withdrawal of his approval and a prohibition?

In essence, the FCA would have to demonstrate the qualitative relevance of Mr Frensham's extra professional conduct to his practice as a financial adviser. The FCA therefore sought to establish a link between Mr Frensham's behaviour and (i) the consumer protection objective; and (ii) the integrity objective.

As regards the **consumer protection objective**, the FCA relied upon an "abuse of trust" parallel argument – on the basis that Mr Frensham's offence involved an abuse of trust and being a financial adviser requires client trust. Beyond that, the FCA placed reliance upon a general assertion that Mr Frensham displayed a willingness to disregard ethical and legal standards that posed an unacceptable risk to consumers and the integrity of the financial services industry more generally. The FCA further relied upon the need to maintain public confidence – on the basis of an assertion that the public are entitled to expect that approved persons are individuals of the utmost integrity and reputation.

The Upper Tribunal was unconvinced by these arguments:

"Those statements appear to be bare assertions and no evidence has been offered to support them ... The assertions … seem to be based only on the awfulness of the offence itself, which we readily accept to be the case. It would have been helpful had the FCA's assertions been backed up by criminological or psychological evidence which could support the view that the serious failure to act with integrity in one's personal life in the manner that Mr Frensham did, by seeking to exploit a young girl, runs a significant risk that he would likewise seek to exploit vulnerable clients (such as the elderly) who seek to rely on him putting his clients' interests before his own when giving them advice …"

With respect to the **integrity objective**, the Upper Tribunal accepted that this embraced public confidence in the financial services industry and in that context whether there is a significant risk that the confidence of consumers will be impaired if it is known that a person guilty of an offence of this nature is allowed to work as a financial adviser. The Upper Tribunal stated that the FCA was *"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. Mr Frensham's personal reputation has clearly been severely damaged as a result of the offence.* ***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 FCA's integrity objective*** *… Furthermore, popular outcry is not proof that a particular set of events gives rise to any matter falling within the regulator's remit."* {our emphasis}

According to the Upper Tribunal, *"the FCA has not clearly linked the facts of the case to the relevant regulatory provision, in this case the integrity objective. They deal with the public confidence question simply by reference to an assertion that the public are entitled to expect that approved persons are individuals of the utmost integrity and reputation. That simply amounts to saying that the offence must be regarded as so awful and would be regarded by fair-minded members of the public with knowledge of the facts, that the only answer to the question posed must*

be that the person concerned must be prohibited from working in the industry. That is presumably because public confidence in the industry would be significantly harmed if such a person was allowed to continue to work in the industry. However, the FCA's guidance does not make it clear that particular offences are considered by the FCA to be so serious that without more they would automatically disqualify the person concerned from working in the industry. ***In those circumstances, the FCA's assertions must be supported by evidence*** *… As with the consumer protection issue,* ***the FCA's case would … benefit from a more independent, analytical justification of the link between the offence and public confidence.****"* {our emphasis}

Conclusion

In summary, in the specific context of Mr Frensham's conviction alone, the FCA had failed to establish the requisite degree of relevance of his conduct with his regulatory fitness and propriety by, in turn, failing to establish the necessary links between Mr Frensham's conduct and the relevant regulatory objectives. In the absence of credible and objective supporting evidence, the FCA's bare assertions proved insufficient.

Case 2: Ashkan Zahedian (2022)

Mr Zahedian[7] was the sole director of an FCA-regulated consumer credit firm and an FCA-approved person. Whilst an approved person, in February 2020, Mr Zahedian was involved in an altercation at a bar, during which he used a machete to assault (and wound) a security guard. He subsequently pleaded guilty to one count of wounding with intent to do grievous bodily harm and one count of possession of a machete in a public place. Mr Zahedian was sentenced to a term of three years' imprisonment.

The judge accepted that Mr Zahedian's actions were out of character and believed that they would not recur. In his sentencing remarks, the judge commented that *"the behaviour of any other person in no way excuses what you did because you chose, and it was free choice, to get a weapon from your car, you escalated things, you lost control, and you caused a nasty wound. Whatever your earlier intention, at the time you intended that wound, you intended to cause him really serious harm."* The judge also noted that Mr Zahedian had been genuinely shocked, ashamed and remorseful as to what had happened.

In a Final Notice dated 14 November 2022[8], the FCA announced that it had decided to withdraw Mr Zahedian's approval and impose a prohibition.

The FCA explained that:

"Given the nature and circumstances of his offending, it appears to the FCA that Mr Zahedian is not a fit and proper person to perform any [regulated] function … His convictions for violent offences demonstrate a clear and serious lack of integrity and reputation such that he is not fit and proper to perform regulated activities ... In our view, there is a severe risk of erosion of public confidence if those who are convicted of violent offences are permitted to continue working in the financial services industry."

Paragraphs 16 and 17 of the Final Notice are set out below:

"16. Given the nature and circumstances of Mr Zahedian's violent offences, this demonstrates a clear and serious lack of integrity. Mr Zahedian caused grievous bodily harm with intent. His conduct amounted to serious criminal offences and he demonstrated a deliberate and criminal disregard for appropriate standards of behaviour. Mr Zahedian was sentenced to three years in prison for the offences.

17. The Authority further considers that the nature of Mr Zahedian's offences and, separately, of the associated publicity following his conviction, is such that he does not have the requisite reputation to perform functions in relation to regulated activities and is likely to damage the reputation of any regulated firm at which he is required to perform such functions. Further, he poses a serious risk of damage to the reputation of, and public confidence in, the financial services sector."

It is evident that, in contrast to *Frensham*, the FCA is here relying solely on an alleged integrity objective linkage.

For reasons unknown, Mr Zahedian did not appeal the FCA's decision. Had he done so, however, it is not clear how the FCA would have overcome the thresholds referenced in the *Frensham* judgement.

- **First**, in arriving at its decision to sanction Mr Zahedian, the FCA provides no supporting evidence to back up the assertions in paragraph 17 of the Final Notice (replicated above) – which are of a similar nature and essence to those made by the FCA when attempting (and failing) to establish the requisite link between Mr Frensham's conviction and the integrity objective.
- **Second** (and transposing the Upper Tribunal's formulation from *Frensham* across to the present case), while Mr Zahedian's personal reputation has clearly been severely damaged as a result of the offence, **the question is whether the offence affects the reputation of Mr Zahedian as a sole director of a consumer credit firm and therefore potentially has an impact on the FCA's integrity objective.** Significantly, the Final Notice references no supporting evidence to link Mr Zahedian's conduct to his *professional* reputation (as was required in *Frensham*).

- **Third**, the FCA does not explain why (and how) the offence perpetrated by Mr Zahedian was relevant to his professional role – as cited by the Upper Tribunal in *Frensham*[9]:

  "It is not simply a question of assessing whether the behaviour concerned demonstrates a lack of integrity at large, but whether the behaviour engages the specific standards laid down by the [FCA][10]*. … Failing to act without integrity in one's personal life in a manner which is not relevant to how the person concerned is required to conduct himself in his professional life should not in itself engage regulatory action."*[11]

- **Fourth**, unlike Mr Frensham, Mr Zahedian's offence did not involve an element of exploitation or abuse of trust – and was, therefore, arguably less germane / concerning in the financial services context.

- **Fifth**, while not condoning or excusing his conduct, Mr Zahedian had seemingly reacted to a provocation of sorts, and it appears that his behaviour was spur-of-the-moment. Mr Frensham's conduct, on the other hand, was of a more pre-meditated nature. Furthermore, as the judge remarked, Mr Zahedian had shown remorse and had acted out of character, such that the judge regarded this as a one-off incident.

- **Sixth**, while the FCA's "*deliberate and criminal disregard for appropriate standards of behaviour*" contention was not subject to any apparent scrutiny in *Zahedian*, it is notable that a similar argument was given short shrift by the Upper Tribunal in *Frensham*.

- **Seventh**, and as a more general point, the FCA's underlying reasoning in *Zahedian* is conspicuous by its absence. On the face of the Final Notice (and without more), it is difficult to see how the various relevance and evidential thresholds referenced in *Frensham* would have been met by the FCA on an appeal by Mr Zahedian before the Upper Tribunal. They are not addressed – fully or at all – in the Final Notice.

- **Finally**, it is interesting to note that the FIT 2.1.1G extract provided by the FCA at the end of the Final Notice[12] omits what is arguably the most relevant (but, for the FCA, most inconvenient) part of all – namely:

  "The FCA should be informed of these matters (see SUP 10A.14.17 R and SUP 10C.14.18R), ***but will consider the circumstances only where relevant to the requirements and standards of the regulatory system.****"* {our emphasis}.

Concluding remarks

We can only speculate as to how *Zahedian* would have been decided by the Upper Tribunal, in the wake of its judgment in *Frensham*. However, as explained, Mr Zahedian's offence was, in various respects, arguably of less relevance – both to his regulated role (given the absence of any element of exploitation or abuse of trust) and to the FCA's statutory objectives (for instance, the FCA not even arguing any linkage to the consumer protection objective). Moreover, Mr Zahedian's offence was not pre-meditated, he showed remorse and would not (according to the judge) reoffend. Indeed, Mr Zahedian may feel somewhat aggrieved if he read the Frensham judgement.

The FCA may have taken a calculated gamble in *Zahedian* – in the hope (or expectation) that it would not be appealed. That risk paid off and the decision was not therefore subjected to Upper Tribunal scrutiny. The FCA may not be so lucky if it pursues similar non-financial misconduct cases in the future – if the defendant decides to appeal and the various *Frensham* thresholds are scrupulously applied.

From a strict legal perspective, firms faced with determining the regulatory relevance of non-financial misconduct incidents perpetrated by employees should apply the *Frensham* thresholds – as that represents the current law, even if it happens not to be to the FCA's liking.

Endnotes

1 https://assets.publishing.service.gov.uk/media/612e14dfe90e07054107585e/Frensham_v_FCA.pdf.

2 14 November 2022. https://www.fca.org.uk/news/press-releases/fca-bans-director-financial-services-violent-criminal-conviction.

3 [2021] UKUT 0222 (TCC).

4 https://www.fca.org.uk/news/press-releases/fca-publishes-decision-notice-against-jon-frensham-non-financial-misconduct.

5 In failing to report certain matters – for instance, the fact of his arrest and his remand in custody.

6 EG 9.2.3.

7 https://www.fca.org.uk/news/press-releases/fca-bans-director-financial-services-violent-criminal-conviction.

8 https://www.fca.org.uk/publication/final-notices/ashkan-zahedian.pdf.

9 At paragraph 41.

10 Paragraph 40.

11 Paragraph 42.

12 *"In determining a person's honesty, integrity and reputation, the FCA will have regard to all relevant matters including, but not limited to, those set out in FIT 2.1.3 G".*

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