

FCA AND PRA CONSULTATION ON DIVERSITY AND INCLUSION IN THE FINANCIAL SERVICES SECTOR

The FCA and PRA (the 'regulators') have published their much anticipated consultation papers ([PRA CP 18/23](#) and [FCA CP23/20](#)) on a package of measures to promote diversity and inclusion (D&I) in the financial services sector with a view to achieving healthier firm cultures, reducing groupthink, unlocking new talent and addressing consumer needs. The regulators clearly regard some of the proposed steps as significant interventions.

The regulators' July 2021 discussion paper ([DP21/2](#)) made it clear that they wanted firms to think about how they can advance D&I through improvements to their policies, governance arrangements, accountability, remuneration arrangements and disclosure. To help inform their proposals a one-off voluntary pilot data survey was carried out in late 2021 culminating in the December 2022 FCA review paper: [Understanding approaches to D&I in financial services](#).

These consultations mark the regulators' next step towards the achievement of greater D&I in financial services and importantly also provide greater clarity on the regulators' expectations around non-financial misconduct (the regulators are seeking to clamp down in particular on bullying and sexual harassment as part of their D&I strategy).

The final regulatory requirements will be set out in a Policy Statement (PS) in 2024. In-scope firms will be subject to the new rules 12 months after the publication of the PS subject to some limited transitional provisions. The regulators have worked closely together to produce consistent and coordinated proposals for consultation albeit that their respective proposals are necessarily driven by the regulators' underlying statutory objectives resulting in some subtle differences.

In broad terms the following policy areas are addressed by the regulators: Non-financial misconduct, D&I Strategies, Data Reporting, D&I Disclosure obligations and setting D&I Targets.

The regulators have not pursued some of the interventions addressed in DP21/2 (such as allocating D&I prescribed responsibility to an individual senior manager). However, given the regulators are painting D&I as a risk issue, formalising rules and guidance, and introducing evidence-based granularity into certain data and reporting requirements, it is clear that if the changes are introduced firms and employees must regard D&I as a systemic regulatory issue.

Key Proposals

- The integration of non-financial misconduct considerations into the regulators' rules on conduct and fitness and propriety assessments and the guidance on the suitability threshold conditions;
- An annual obligation to report employee numbers;
- A requirement to set targets to address underrepresentation at Board, senior leadership and general workforce level;
- An annual D&I reporting obligation;
- A requirement to publish D&I strategies;
- Individual accountability under the SM&CR and remuneration alignment (PRA only).

The package of measures proposed in the consultation papers ([PRA CP 18/23](#) and [FCA CP23/20](#)) is broad. While this Briefing provides an overview we have prepared separate 'deep dive' Briefings on focus areas. Our Briefing [Non-Financial Misconduct: D&I in Financial Services Consultation](#) examines the key proposals in respect of non-financial misconduct and our Briefing [D&I in Financial Services Consultation](#) examines the key proposals in respect of D&I Strategies, Data Reporting, D&I Disclosure obligations and setting D&I Targets.

WHAT FIRMS ARE IN SCOPE?

In keeping with the regulators' approach to proportionality firms will be subject to different proposals depending on the number of employees, their Senior Managers and Certification Regime (SM&CR) categorisation and whether they are dual-regulated. Smaller firms with fewer than 251 employees will be exempt from many of the requirements.

FCA CP 23/20 provides that a minimum standard will apply to all FSMA firms with a part 4A permission in relation to the proposals on: 'non-financial misconduct' and 'Data Reporting' and additional rules on D&I Strategies, Data Disclosure, Setting Targets and Risk and Governance (see further below) will apply to firms with 251 or more employees (so called 'large firms').

The PRA's CP18/23 proposals apply only to Capital Requirements Regulation (CRR) firms and Solvency II firms (which includes third country bank and insurance branches) with a similar proportionality approach being taken in respect of smaller firms. No proposals apply to non-CRR and non-Solvency II firms (e.g. credit unions and friendly societies).

What is a large firm?

As mentioned above a firm with 251 or more employees will be 'a large firm' for the purposes of the proposed additional requirements. The average number of employees over a rolling 3-year period as at a specified annual reference date will determine whether the employee threshold is met. For these purposes firms must have regard to the regulators' wider definition of employee that may require contractors, individuals seconded to the firm and non-executive members of the board to be considered.

KEY POLICY PROPOSALS BY FIRM TYPE

Policy areas	Which firms the proposals apply to
Non-Financial Misconduct	All FSMA Firms with a Part4A permission and where relevant Threshold Conditions and existing chapters of the Handbook apply (including COCON and FIT)
	All CRR and Solvency II firms with respect to their establishment in the UK, including third country branches
D&I Strategies	All CRR and Solvency II firms of any size with respect to their establishment in the UK, including third country branches
	All FSMA firms with a Part 4A permission who have 251 or more employees, excluding all Limited Scope SM&CR firms (' Large FCA Firms ')
Risk & Governance	All FSMA firms with a Part 4A permission with 251 or more employees, excluding all Limited Scope SM&CR firms (' Large FCA Firms ')
	All CRR and Solvency II firms with respect to their establishment in the UK, excluding third country branches
Data Reporting D&I Disclosure Setting D&I Targets	All FSMA firms with a Part 4A permission need to report their number of employees annually, excluding all Limited Scope SM&CR firms
	All FSMA firms with a Part 4A permission with 251 or more employees have additional reporting obligations, excluding all Limited Scope SM&CR firms (' Large FCA Firms ')
	Only those CRR and Solvency II firms (including third country branches) with 251 or more employees who are predominantly carrying out activities from an establishment in the UK All FSMA firms with a Part 4A permission with 251 or more employees have additional reporting obligations, excluding all Limited Scope SM&CR firms (' Large FCA Firms ')

PREPARATORY STEPS

Firms would be advised to consider:

- what their current D&I data collection, practices and policies look like and what current difficulties they encounter;
- how they currently approach non-financial misconduct;
- what the practical and legal implications of the proposals outlined might mean for, amongst other things, their:
 - policy, governance, specific infrastructure (ownership by relevant committees, review processes, KPIs and incentivisation);
 - remuneration arrangements;
 - annual review and certification and related HR systems (including the extent to which non-financial misconduct is considered);
 - employee engagement surveys and training;
 - operational and senior manager oversight (of for example D&I strategy, implementation and workplace culture); and
 - data collection processes.
- what areas of the firm currently 'own' matters relating to D&I and non-financial misconduct (such as designated Senior Managers, HR or People & Culture/ D&I leads) and whether that may need to be expanded to include, for example risk and audit;
- what consultation may be needed with key internal stakeholders when the changes are finalised (and making senior managers and relevant operational areas aware changes are in the pipeline);
- developing early communications campaigns that frame the purpose of the D&I strategy and any targets.

Once the final Policy Statement is published firms will want to carry out a deep dive to ensure that they have the frameworks, culture, training and processes in place across the firm to ensure that they can comply with this regulatory 'intervention'.

[Diversity and inclusion in the financial sector DP21/2](#)

[FCA Understanding approaches to D&I in financial services](#)

[FCA CP 23/20 Diversity and inclusion in the financial sector – working together to drive change](#)

[PRA CP 18/23 Diversity and inclusion in PRA-regulated firms](#)

[Briefing: FCA and PRA Consultation on Diversity and Inclusion in the financial services sector: Non-Financial Misconduct](#)

[Briefing: FCA and PRA Consultation on Diversity and Inclusion in the financial services sector: D&I Strategies, Reporting, Disclosure Obligations and Targets](#)

TIMETABLE/NEXT STEPS

- Responses to the consultation paper can be submitted until **18 December 2023**.
- The FCA/PRA Policy Statement will be published in 2024 and the implementation date for changes will be 12 months after publication of the Policy Statement to give firms time to prepare.

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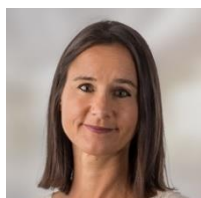
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