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Insights

NON-FINANCIAL MISCONDUCT REGULATION – REGULATORY OVERREACH, OR PROGRESSIVE RISK MANAGEMENT STRATEGY?

Jan 26, 2026

On 12 December 2025, the FCA published its long-awaited Policy Statement PS25/23: Tackling non-financial misconduct in financial services, finalising its formal Handbook guidance on non-financial misconduct.

The new guidance, which amends the COCON and FIT sourcebooks in the FCA Handbook, will take effect on 1 September 2026. Firms now have less than nine months to prepare for one of the most significant shifts in conduct regulation since the introduction of the Senior Managers and Certification Regime (SMCR).

REDEFINING NON-FINANCIAL MISCONDUCT: A WELCOME RESET

The FCA's definition of the types of conduct falling within scope of the its non-financial misconduct regime articulated in PS25/23 has evolved significantly since the original formulation.

The FCA first introduced draft guidance on how non-financial misconduct fits within its Conduct Rules framework and fitness propriety test in a short annex to Consultation Paper CP23/20 on diversity and inclusion, published in September 2023. In that paper, the FCA proposed defining non-financial misconduct as behaviour "inconsistent with a good working environment, being an environment in which each employee: (1) feels respected, valued and able to give their best; and (2) is treated fairly and with dignity and respect." This initial formulation was widely criticised as unacceptably vague and subjective, raising concerns that it could draw minor HR issues into the regulatory remit.

In its next consultation, CP 25/18, published in July 2025,the FCA replaced its earlier definition with one more closely aligned to employment law principles, reflecting feedback from the 2023 consultation. This updated approach was further refined and finalized in the 2025 consultation, defining non financial misconduct as conduct in relation to an individual colleague, "B", "that has the purpose or effect of: (i) violating B's dignity; or (ii) creating an intimidating, hostile, degrading,

humiliating or offensive environment for B; or (b) conduct that is violent to B." The definition includes both subjective and objective elements:

a. The conduct must have had the effect of making someone feel offended (a subjective test); and

b. It must have been reasonable for that person to have felt offended (an objective test).

Introducing the objective test narrows the scope of the provision, aligning it more closely with employment law standards.

Other improvements made to the draft Handbook guidance since the July 2025 consultation include:

- Removing a controversial suggestion by the FCA that firms report all serious third-party allegations concerning misconduct in staff members' private lives, notwithstanding that "a firm has not been able to establish the truth of an allegation";
- Clarifying that managers will not be held accountable for failing to prevent non-financial misconduct by others where they could not reasonably have known about the misconduct or did not have authority to intervene.

NON-FINANCIAL MISCONDUCT REGULATION WITHIN THE GOVERNMENT'S GROWTH AGENDA

As discussed in the related article, the recent government directives to the FCA have been clear: scale back regulation to drive growth. The government has explicitly targeted the SMCR for reform, seeking to reduce the burden by up to 50% to make the UK a more attractive destination for business.

While the FCA appears to be embracing this instruction, the regulatory changes introduced in PS25/23 appear to be an outlier. Rather than scaling back, they broaden the scope of matters that are subject to FCA conduct regulation and increase individual accountability. Although we support the FCA's goal of fostering ongoing cultural improvement within financial institutions, we highlight two examples of specific non-financial misconduct below that may prove problematic and could be scaled back in future FCA revisions to the Handbook.

PRIVATE LIVES

PS25/23 confirms that while the Conduct Rules focus on workplace behaviour, the Fitness and Propriety (FIT) assessment extends into an Senior Management Function's (SMF) private life whenever the issue could reasonably be considered relevant to their integrity or reputation. Under the new COCON 1.1.3G(2), SMFs must disclose information concerning their private and personal lives to their employers, or to the FCA, if it is material to assessing their fitness and propriety.

This development is perhaps unsurprising given the FCA's recent enforcement fine against Kristo Käärmann, CEO of Wise. In October 2024, Mr Käärman was fined £350,000 for failing to notify the FCA that he had struggled to keep on top of his personal UK tax affairs while living between the UK and overseas, resulting in being added to HMRC's defaulter's list — despite promptly paying all relevant fines to HMRC. In announcing this fine, the FCA stated "It should have been obvious to Mr Käärmann that he needed to tell us about these issues which were highly relevant to our assessment of his fitness and propriety". By all accounts, it was not obvious to Mr Käärman that he owed such a duty, and we would argue that prior to this case, it would not have been particularly obvious to other people either. This new provision creates an unusual degree of personal regulatory exposure for senior management function holders arising from matters unrelated to their financial services work, raising questions about whether this aspect of the new non-financial misconduct guidance genuinely aligns with the government's growth and competitiveness agenda.

"BYSTANDER" RISK

PS25/23 introduces a new liability for managers. The guidance states that a manager may be in breach of Conduct Rule 2 ("You must act with due skill, care and diligence") if they fail to take reasonable steps to prevent or address non-financial misconduct in their teams.

This creates a positive regulatory duty upon managers to prevent non-financial misconduct, similar to the legal duty created for firms in October 2024 requiring firms to take proactive steps to prevent sexual harassment.

In introducing this new guidance, the FCA is clearly seeking to drive proactive cultural change through personal regulatory accountability. In principle, this seems reasonable. However, if if these rules translate into enforcement outcomes against individuals (as was the case with Mr Käärman), and in this case for misconduct that was committed by others, the prospect of taking UK-based senior roles may become less attractive. It would be more appropriate to make non-financial misconduct and broader cultural change a supervisory matter between the FCA and regulated firms, other than in egregious or deliberate cases where clear blame exists.

NOTE TO THE LLOYD'S OF LONDON INSURERS

For our clients in the Lloyd's market, we are still awaiting the final outcome of the Lloyd's of London byelaw review. We understand that Lloyd's had paused their review until the FCA's position was finalised. Now that PS25/23 is published, we expect Lloyd's to release an update in the first half of this year.

EMERGING THEMES

Are you ready for the FCA's new rules on non-financial misconduct? View

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