

The FCA's 5 Conduct Questions: The 1st Line of Defence Perspective

Presentation to 1LOD Summit

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Introducing the 5 Conduct Questions

- Wholesale Banking Supervision has two primary objectives for its sector:
 - To mitigate conduct risk in the sector, and
 - To improve the capacity of the sector to mitigate conduct risk itself
- The 5 Conduct Questions (5CQ) were designed to:
 - Provide a consistent framework that firm supervisors can use to discuss progress firms are making in the development of their Conduct Risk Frameworks
 - Stimulate debate and action within firms and across the industry
 - Provide a mechanism for feedback to industry
- Firms have responded positively to the initiative
- The 5 Conduct Questions have now been rolled out and lessons learned from the first year communicated
- The 1st Line of Defence is at the heart of a great deal of this work and we welcome the advent of this conference to further cement that
- In principle, the 5 Conduct Questions may well be valuable to a much wider audience than wholesale banks

The 5 Conduct Questions are:

1. What proactive steps does the firm take to identify the conduct risks inherent within its business?
2. How does the firm encourage the individuals who work in front, middle, back office, control and support functions to feel responsible for managing the conduct of their business?
3. What support, broadly defined, does the firm put in place to enable those who work for it to improve the conduct of their business/function?
4. How do the Board and ExCo (or the Branch Management) gain oversight of the conduct of their organisation and consider conduct in their deliberations?
5. Has the firm assessed whether there are any other activities that it undertakes/ways in which it operates that could undermine strategies put in place to improve conduct?

Conduct risk needs to be managed wherever it arises within the firm

Some of the things firms found to be effective

- Highly visible CEO sponsorship with engagement and challenge by the Board
- Senior executives (1st and 2nd LoD) taking leading roles in programme design
- Programmes that cover both front office and control functions
- Clear ownership and responsibility for programme implementation by senior business executives, sometimes supported by conduct specialists within the organisation
- Use of a standardised conduct risk self-assessment process across the firm
- A firm-wide taxonomy for conduct risk types enabling consistent data capture and reporting
- A forum for comparison of conduct risks across business lines and functions
- Training, promotion, performance management and remuneration all linking to conduct and culture objectives
- Long-term conduct risk initiatives becoming fully embedded in business as usual

First Line of Defence: Some Tactical Considerations

- Read across is a word commonly used:
 - More simply put, it is good conduct risk identification
 - It requires coordination and cooperation across business lines, functions and sometimes regions
- Systems and controls should exist for one purpose:
 - So that they work
- Careful consideration of what actually needs to be monitored:
 - What is the most appropriate, not necessarily the most convenient, indicator?
- It is important to recognise that human behaviour evolves as it is observed and so conduct risks will evolve as well:
 - This may have implications for the evolution of controls and MI and for upward reporting

First Line of Defence: Some Strategic Considerations

- Embedding conduct risk management across the firm is critical
 - It requires partnerships across the firm and consistency
 - How can the 1st LOD play a role in fostering this?
- How is the strategic direction of the firm aligned to the development of the approach and resources of the 1st LOD?
 - Strategic business developments and the controls environment should seek to evolve in lock-step
- The greater evolution of the 1st LOD is welcomed but can result in blurred lines between the 1st and 2nd Lines of Defence
 - There is also the potential for a blurring between the 2nd and 3rd Lines of Defence
 - How do we ensure the lines are clearly drawn, articulated and maintained?
- Technological evolution is both the 'saviour' and the 'danger' to compliance, creating more tools but potentially more risks
 - The capacity building required to govern technology effectively is required across all 3 Lines of Defence

Thank You



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