

18 December 2023

Governance and Cross-Cutting Standards Policy Team
Financial Conduct Authority
12 Endeavour Square
London
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Dear Governance and Cross-Cutting Standards Policy Team,

Consultation CP23/20 - Diversity and inclusion in the financial sector – working together to drive change

We welcome the opportunity to respond to the consultation document, published by the FCA in partnership with the Prudential Regulation Authority (PRA), on diversity and inclusion in the financial sector.

The Pensions and Lifetime Savings Association (PLSA) is the voice of workplace pensions and savings. We represent pension schemes that together provide a retirement income to more than 30 million savers in the UK and invest more than £1.3 trillion in the UK and abroad. Our members also include asset managers, consultants, law firms, fintechs, and others who play an influential role in people's financial futures. We aim to help everyone achieve a better income in retirement.

In our response, we have taken the approach of grouping some questions so that our response is considered by certain key themes. Where we have done so, we've set out which questions we have grouped together.

Overarching approach – proportionality / definitions (Questions 2, 5 and 17):

We would firstly like to acknowledge that this consultation is a positive start point in ensuring greater consideration and awareness of the importance of diversity and inclusion (D&I) across the financial sector. We understand that all firms will be on different stages of their D&I journey, and not all will be perfect from day one. But these proposals are an important step in supporting firms to strive for continuous improvement. In our response, we urge the FCA to consider how they will further develop their requirements over time to help firms in integrating any proposals that are taken forward.

We support the overarching approach of requiring firms to meet minimum standards to carry on regulated activities and we think it is important that a lack of D&I is treated as a non-financial risk. Embedding rules around non-financial misconduct into FIT (Fit and proper test for employees and senior personnel), COCON (code of conduct), and COND (threshold conditions) will be a positive intervention that will go some way to ensuring that D&I is given the consideration it needs. We question what would happen to firms who are deemed not to be doing enough and would welcome clarity from the FCA on how such firms could face enforcement action and what that would look like.

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We broadly agree with the proposed proportionality framework. It is understandable that, at least initially, smaller firms are not required to adhere to the same rules as larger firms. Our engagement has highlighted that the burden on small firms to adhere to detailed reporting and disclosure requirements would be significant and we know that because of the numbers within small firms, their data input would be statistically insignificant.

That being said, we do want to see the FCA go further and be more ambitious in their approach to tackling D&I issues. As we will outline throughout our response, it is vital that the FCA provide further information on how they intend to develop their approach in time.

1. In relation to requirements on large firms to report and disclose employee information. We would like clarity on:
 - a. How the FCA will drive better engagement with reporting which we know is a challenge many firms face.
 - b. How the FCA will explain why they are collecting this data to overcome distrust issues which can lead to low employee engagement.
2. With regards to the specific characteristics that firms are required to report on, it is vital that the FCA outlines how it will develop and build on its proposed approach to D&I. We would like to know:
 - a. Whether the FCA plans to move towards further mandating of characteristics so that there is not a distinction between compulsory and voluntary reporting.
 - b. How the FCA will support firms to deal with the challenge of poor employee engagement to facilitate good levels of reporting. It is vital that firms develop a representative view of their employees that they can use to drive change.
3. It is important that more information is provided outlining what the FCA want to achieve with its approach to D&I. Our view is that the proposals as drafted lack a clear framework. This could lead many to think that the FCAs view is that data is the solution. However, we know that effective D&I policy is about so much more. Effective data collection is a start point and we want the FCA to outline what values, cultures and behaviours they want to foster through diversity strategies and target setting.
4. Small firms face a number of barriers to effective data collection and reporting. We would like the FCA to consider and clarify whether there is an ambition for further requirements on small firms in time and how they would be supported to engage more effectively with those additional D&I requirements. With barriers in mind, the PLSA feel it is important small firms still do mandatory reporting. A phased timeline incorporating reporting on a comply or explain basis could be part of this approach.
5. Finally, we are interested in understanding in more detail what consequences firms will face if a bad actor is identified. Clearly, we hope that enforcement action is not required, but in some circumstances, it may be necessary.

We would like to emphasise that the PLSA is determined to support our members and the wider financial services industry to improve diversity and inclusion. We are very willing to work with the FCA to consider how best to engage employees and to be a part of any marketing or campaigning that seeks to drive increased engagement in D&I reporting.

Data reporting and disclosure (Q4, 6, 12, 14, 15, 16)

While we understand the rationale behind small firms not being required to report any data, other than their number of employees initially, it is vitally important that in time, the FCA sets out

proposals for how small firms could report on diversity and inclusion and that they outline how they will support small firms to play a more active role in the reporting and disclosure of data to achieve their D&I objectives. It sends the wrong signal otherwise, that small firms are exempt from thinking about D&I and could be an impediment to a full industry movement towards a true cultural shift that the FCA is, we believe, aiming for.

As well as urging the FCA to consider their approach to small firms, it is also vital that large firms are supported to meet the proposed regulatory requirements. The FCA proposes that large firms be required to collect certain data relating to the characteristics of their employees. Firms will then be required to disclose that information publicly. Whilst we support this approach to reporting and disclosure, our members have told us that they have concerns around existing levels of employee engagement when it comes to reporting personal information. FCA have made clear that there will be an option for employees to indicate that they do not wish to disclose certain personal information (without the firm being sanctioned). We ask the FCA to clarify what the employee reporting exemption means in practice.

Implementing an exemption, where employees do not have to report information if they do not want to, does not help to shift attitudes on the value of engagement with D&I policies. The FCA does not propose setting targets relating to what they deem to be an appropriate level of reporting. In addition, the FCA does not outline what role it sees itself undertaking in terms of supporting firms to improve employee engagement. We therefore ask the FCA to clarify:

1. What they deem to be an appropriate and meaningful level of reporting.
 - a. Whilst we acknowledge that having mandatory and voluntary characteristics initially (and only requiring reporting on mandatory items) is helpful, we do want the FCA to outline what they deem an appropriate level of reporting. We also ask for clarification on whether the FCA will consider setting reporting targets, and moving towards mandatory reporting and disclosure of all listed characteristics in time (and if so, how).
 - b. We believe that doing so could have the effect of shifting the dial on attitudes towards reporting. If it becomes the norm for employees to report a comprehensive suite of personal information, and they see that in doing so, it has a positive effect on the ability of their employer to effectively support them, there is the potential for great progress to be made on D&I.
 - c. As a short-term solution, we would like to see firms providing greater assurances on how employee data will be used and confidentially stored. It would be beneficial for firms to have access to FCA guidance on how to communicate this, and how to ensure confidentiality in a logistical sense.
2. What they will do to support firms to improve employee engagement with reporting.
 - a. We are concerned that in the absence of FCA support, there will be significant pressure on firms to achieve effective levels of reporting with no clarity on how they do this, or whether their efforts are enough to achieve meaningful levels of reporting.

Additionally, recruitment research shows that younger cohorts in particular prioritise D&I, and if policies and reporting are not made publicly available, they are less likely to apply for roles within those companies. In turn, firms will lose out on talent and on the choice from a more diverse pool of applicants. But, because mandating all characteristics will pose challenges, work is needed to explain to employees why it is important and what the FCA want to achieve. We want the FCA to work with firms to help build employee trust and support in the value of reporting. This will help

them to understand that reporting is one way that they can help to bring about change within their organisation.

We support the FCA approach of mandating the reporting and disclosure of some characteristics over others initially. We think that will help to make employee engagement easier. We are broadly supportive of the approach that will see firms required to disclose the same data that they report. Transparency is vital and disclosing all reported information that is mandatory will allow for effective comparisons across the financial services sector.

Characteristics (Q10, 11)

As we have outlined, when it comes to the specific characteristics that the FCA proposes, large firms should report on and disclose, we are supportive of the proposed approach and the rationale behind separating mandatory and voluntary characteristics, at least initially. We would like the FCA to outline in more detail how it will move towards further mandating of characteristics in time. We do have concerns with some of the characteristics themselves which we strongly encourage the FCA to consider in more detail:

1. We believe 'disability' is a poor descriptor. Our membership has expressed a desire to see this broken down further. One way to do that could be to look at 'physical impairment' and 'neuro-divergence'. It is crucial to get this right as people must recognise themselves in the characteristics they are asked to report on. We would recommend ensuring language and terms are aligned with effective language that has already been established in legislation. If necessary, the FCA should work with experts in the health and disability sector to get this right.
2. We are concerned that for data provided on caring and parental responsibilities, one is only getting a snapshot of how that person is coping with their responsibilities at any given moment in time. From an inclusion perspective, firms must be mindful of the fact that how people are coping will change numerous times throughout the year.
3. We would like to see socio-economic background considered as a mandatory characteristic to report. Having this information is a vital way of understanding employees better and is crucial in ensuring effective representation of a firm's range of customers.
4. Further to our concerns on inclusion, we think it is important that recognition is also given to how employees with different working patterns (full time vs part time/compressed hours workers/differing shift patterns) or how workers under different types of contracts (including zero hours) experience inclusion in the workplace.
 - a. It can often be the case that there is less attention given to the contributions of those who are not as frequently physically present because of their working hours.
 - b. In addition, our [2021 report with Railpen](#) analysing workforce reporting highlighted that companies should report equally on workers under all contract types, not just their direct employees.
 - c. We urge the FCA to clarify whether reporting these different experiences will be considered to ensure a complete picture is developed across firms.

Next steps: Proposals for large firms – strategies and target setting (Q7, 8):

At the start of the consultation paper, a set of preferred outcomes have been identified. Achieving healthier firm cultures, reducing groupthink, unlocking new talent, and achieving a greater understanding of, and provision for, diverse consumer needs. These are all positive and great reasons to strive for greater D&I. However, the emphasis on data reporting and disclosure could

lead many to think that the FCA see the solution as being a simple one – gather more data. As we have outlined, data alone is not enough. Data is crucial in shaping how firms plan and take action to support their employees, but fundamentally, and underpinning everything, is what firms do with that data.

Parallels could be drawn to ongoing industry efforts in relation to climate change. The destination, net zero, is clear and with an increasing emphasis being placed on transition plans to guide organisations to get there, we see structure being put in place. This consultation proposes a flexible and proportionate approach. We support that, ultimately, it should be for firms to dictate their own D&I strategy and set targets that align with their own priorities. But this consultation is lacking a greater understanding of what the FCA want to achieve. Unlike with climate change, the end goal is not clearly specified. It would be helpful for the FCA to set out what good looks like and how they will encourage and support firms to achieve these standards. This will provide firms with vital clarity to shape their approach. The FCAs proposals around requiring firms to develop evidence-based D&I strategies and setting targets to address underrepresentation are positive. However, these proposals could be made more robust with additional support put in place to demonstrate the FCAs preferred direction of travel.

- The FCA does not propose stipulating how frequently the strategies should be reviewed. Whilst it is expected that they will be regularly reviewed to ensure they remain fit for purpose, that is not guaranteed. It would be worth considering whether a requirement to review D&I strategies at prescribed intervals will help the FCA to achieve its objectives.
- The FCA proposes requiring firms to set targets to address underrepresentation in their firms. The FCA will not stipulate how frequently targets should be reviewed and updated, and again, we would like the FCA to consider whether this goes far enough in supporting them to achieve their objectives.
- Target setting is not simple. Achievable targets need to be set by considering both evidence gathered, and ambitions of what firms want to achieve. Some further guidance from the FCA on what firms should consider when setting targets would be welcomed by a lot of firms.
- The FCA outlines how one of the challenges firms face in relation to diversity is that different groups of people may be less likely to access different financial products. We think that it would be beneficial for the FCA to conduct research exploring the reasons for this. Having this information could be beneficial to firms when it comes to tailoring their strategies and targets appropriately.
- We urge the FCA to re-consider its approach in relation to several important proposals that have been parked:
 - Training – the consultation outlined that specific proposals on training would not be brought forward because of the mixed feedback on the effectiveness of it. As we have already reflected on, we heard concerns that the FCA proposals will not do enough to bring about changes in culture or behaviours. As an example, there were concerns that unconscious bias training has become stale and does not work on a stand-alone basis. Encouraging changes to the way training is delivered could be an effective way for the FCA to demonstrate that it is focused not just on collecting data but using it to take meaningful action to improve firms.
 - Talent pipelines - Building on our concern that not enough is done to consider what firms do with their data, we think the lack of emphasis on talent pipelines is an issue. High costs and the desire to avoid unnecessary prescription in areas where many firms already have

well-established approaches has been cited as to why this is the case. But our feedback suggests that more opportunities are needed and given the high costs of reporting requirements, it would be helpful to understand why the lines have been drawn in the way they have to leave out further work on talent pipelines.

- Individual accountability – the consultation suggests that because firms are already required to record SMF responsibilities in their SoRs, the FCA is content that there are sufficient mechanisms in place to ensure responsibility for D&I progress. This appears to contradict with discussion paper feedback calling for a clear tone from the top of firms with clear responsibilities indicated. In addition, we heard that individual accountability is vital in ensuring ownership is taken for driving progress.

Additionally, we do have concerns that the publication of targets could have unintended consequences. The FCA must engage with firms to ensure that D&I strategies and targets are ambitious and drive the positive outcomes that we would expect. There is a risk that they become conservatively managed because they are public and this would not be a good outcome.

Inclusion (Q13):

When it comes to inclusion, we support the FCAs proposals to include certain questions within its proposed regulatory return requirements. If this data is returned effectively, and at scale, it will be a useful way to monitor how employee experiences. We do think there are issues however with the way the questions are framed:

- We are concerned about the wording of the proposed questions. They are negative in tone, and we think it would be beneficial to work with behavioural science experts to re-frame them and drive a more engaged response.
- The questions at present are too open ended. To get a sense of employee experiences over time, the questions need to make clear what period you are asking them to consider. Is it in the last 6/12/18 months?
- It is vital that the inclusion questions are standardised across firms so that they are comparable. We would be grateful if the FCA could confirm that they will prescribe the specific questions so that responses are able to be compared.

We have also heard concerns around what decisive actions can be taken to achieve the FCA's D&I aims. The FCA wants to foster innovation, talent, fresh ideas and reduce groupthink, but more needs to be done to outline how that will happen. The cycling in of new talent at board level to increase innovation, reduce groupthink and prevent staleness in thinking would be invaluable to many firms. The lack of emphasis on talent pipelines is a concern. Opportunities must exist to support individuals to progress and develop to more senior positions so that boards are more statistically representative of the customer base. In addition, the FCA could consider whether there should be maximum terms on boards. We would welcome further information from the FCA on whether there is anything being considered.

Our overarching concern however is that at present, inclusion does appear to be a lower priority and we think it must be given greater prominence within the proposals. We are concerned that inclusion measures are being based solely on employee engagement questionnaires. For example, with regards to target setting, it is currently proposed that any targets on inclusion would be optional. A positive step could be to consider whether at least one inclusion target could be mandatory. At present, it feels as though diversity and inclusion are being considered in isolation

when we know that improving inclusion is vital in facilitating greater diversity, as at the heart of progress in D&I, there has to be a fundamental shift in cultural and organisational attitudes towards the principles of diversity.

Costs (Q18):

The cost benefit analysis indicates that the startup cost for the proposed requirements is £0.5bn with £0.33bn each year in ongoing costs (increase of 8% per year on ongoing costs). While our members have placed D&I as a priority, some have also acknowledged that this is a significant cost and we know that there is, for now, conflicting evidence around whether there is a business case for prioritising D&I. Any further changes in approach will need to be carefully managed to ensure costs do not become unmanageable for firms. Our view however is that the promotion of D&I is the right thing to do and should be promoted irrespective of the costs. There is certainly a strong desire for change amongst our membership and we are encouraged by the FCA prioritising this important issue.

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We thank the FCA for the opportunity to respond to this consultation and we urge further consideration of the issues we have raised in our response to shape final FCA and PRA proposals on introducing a new regulatory framework on D&I in the financial sector. We would be happy to respond to any queries or provide further information.

Kind regards,

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