SQUIRE PATTON BOGGS

The intersection of employment law and financial regulation: Addressing non-financial misconduct (NFM)

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The Financial Conduct Authority's (FCA) new rules on NFM will come into force on 1 September. This will have a large impact on non-bank institutions. All firms regulated by the Senior Managers and Certification Regime (SMCR), and not just banks, must prevent unwanted conduct in the workplace even if it does not directly relate to regulated activities. This is a big shift; previously, the rules around unwanted conduct related to a non-bank's regulated activities. Non-banks must soon take steps to prevent bullying, harassment or violence against colleagues where this is related to work. The handbook guidance (PS25/23) was published to help firms better understand their obligations.

This comes following years of consultation and consideration by the FCA on how to tackle NFM and drive systemic change in financial services firms, which have historically been perceived as problematic. This rule change does not have retrospective effect.

Financial Services (FS) firms are navigating a period of unprecedented regulatory and legislative convergence. The FCA's NFM rules will be followed just weeks later by a materially strengthened sexual harassment duty on 30 October. Together with recent changes on the prohibition of non-disclosure agreements (NDAs) and sexual harassment now being classed as a qualifying disclosure for whistleblowing purposes, the days of managing harassment complaints quietly would seem to be coming to an end. This is in addition to a raft of changes being brought in by the Employment Rights Act 2025, including the doubling of the time employees have to bring employment tribunal proceedings from October 2026, and from 1 January 2027, reducing the required service to bring unfair dismissal claims to six months (as well as the removal of the compensatory award cap).

1 September 2026: NFM changes

The September rule change relates to the introduction of COCON 1.1.7FR, which brings non-banks into scope of NFM. What does this mean? It means that employees working in non-banks must not carry out NFM in the performance of their duties, and that this is no longer limited to regulated activities only. This means in turn that HR, legal and compliance teams sitting in non-banks must be alive to the fact that employees' actions could well constitute NFM. What this necessarily entails in practice is that firms will be required to investigate misconduct where they feel the requisite criteria have been met (see below). This is the tricky part that will necessarily require some degree of trial and error.

Only if a finding that requires formal disciplinary action is made, should the FCA be informed. This leaves firms in an understandably conflicted scenario in needing to gauge and assess conduct against the regulatory threshold while remaining objective, so as to not jeopardise their own operations and individuals' professional lives.

The test for NFM is now aligning more closely with the definition of harassment under the Equality Act 2010, though no protected characteristic is required. NFM is defined as unwanted conduct that either: (i) has the purpose or effect of violating a colleague's dignity or creating an intimidating, hostile, degrading, humiliating or offensive environment for that colleague; or (ii) is violent to that colleague.

When assessing NFM, the FCA will have regard to several factors, including:

- Whether the conduct formed a persistent and recurring pattern of behaviour
- The sustained period over which it occurred
- The gravity of its consequences for anyone affected
- The authority/position held by the wrongdoer within the firm, and whether the individual demonstrated a lack of candour or acted in bad faith
- The extent to which any previous warnings have been given

Our previous blog explored the FCA's final guidance in 2025, and summarised the key factors the FCA will look out for. Firms are encouraged to implement training prior to the rule change so that all employees are clear on how this rule change impacts them.

In addition to the NFM changes, it is important to highlight the overlap with recent and upcoming revisions to employment law. The combined effect of this strengthened regime means that firms operating in the FS sector must be more prepared than ever to manage their employee workforce, as well as investigate and discipline misconduct appropriately.

Over the course of the year, it has become clear that several developments will impact the NFM regime:

1. **Use of NDA clauses** – On 6 January, contractual clauses preventing workers from speaking about harassment or discrimination became void. This will have some bearing on NFM as it removes the use of NDAs as a tool to manage misconduct quietly, which has historically often been the case.

2. **Sexual harassment may now receive whistleblowing protection** – Sexual harassment allegations became capable of being classed as a protected disclosure on 6 April. An employee who has raised a concern about sexual harassment, whether internally or externally, may now be afforded full legal protection as a whistleblower, including the right to claim unfair dismissal from day one and uncapped compensation (from 1 January 2027). Firms that subject an employee to detriment for raising such a concern may face claims, but where a manager is concerned, there may also be a breach of the COCON rules, creating double exposure.

3. **Doubling of employment tribunal litigation limitation period** – From 1 October, the limitation period to bring an employment tribunal claim will increase to six months. This means that where an employee in an FS firm raises a grievance about bullying, harassment or other NFM, and is subsequently dismissed or subjected to a detriment, the exposure on a business is increased as they have double the time to bring Tribunal proceedings.

4. **Increased sexual harassment prevention duty** – The FCA's manager obligations to take reasonable steps to prevent NFM sits separately to, but alongside, the employer duty to prevent sexual harassment. This will from 30 October be strengthened to a higher standard; a duty to take "all reasonable steps" to prevent sexual harassment. FS firms will therefore have two parallel prevention obligations – one regulatory and one under employment law. Their failure to do so can allow an employee a 25% compensation uplift should their claim be successful and deprive an employer of the defence it otherwise could show.

   This is consistent in that prevention must be systematic and evidenced. Robust policies and training will be paramount.

   In addition, from the same date, employers may be directly liable if a worker is harassed by a third-party such as a client or contractor, which means that for FS firms where client entertaining or other interaction is common, this is a significant new risk area that firms need to be alive to.

5. **Lastly, from 1 January 2027, the requisite service for unfair dismissal claims will drop from two years to six months, and the compensatory award cap for unfair dismissal claims will be removed** – This creates a real risk for firms where high earners/senior individuals are dismissed. This cap is currently £118,223 or 52 weeks' gross pay, whichever is the lower. For FS firms, the cap removal materially increases the potential financial exposure in dismissal disputes, particularly where executives are easily earning six to seven figures. There is also an interaction with NFM, where an executive is investigated for NFM and later dismissed, the process followed can and will be scrutinised both from an employment law unfair dismissal perspective but also from a regulatory perspective.

This is a period of real change, particularly for those operating in the FS sphere.

Firms are encouraged to review and, where appropriate, update their policies, conduct breach reporting, approach to fit and proper assessments and regulatory references. Historic fitness and propriety assessments do not need to be reviewed.

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