

Governance and Cross-Cutting Standards Policy Team
Financial Conduct Authority
12 Endeavour Square
London E20 1JN

Response by email to CP23-20@fca.org.uk

15 December 2023

Response to FCA CP23/20 Diversity and inclusion in the financial sector

We, the Association of Real Estate Funds¹ (AREF), welcome the opportunity to respond to the FCA's consultation on diversity and inclusion ('D&I') in the financial sector. Our membership is made up of real estate funds that are managed mainly by large firms with over 250 employees. Also, we have Affiliate members, that support the real estate funds sector; these are firms of various sizes and are not all within the UK; some are based in the Channel Islands. Our members will be better placed to answer in detail the questions within the consultation. However, AREF would like to give our support for this initiative.

One of AREF's key aims is to encourage its Fund Members to adopt the highest possible standards of transparency and corporate governance. This is achieved by Fund Members confirming they follow the requirements within AREF's Code of Practice. Fund Members are expected to provide transparent, unambiguous and timely information, as stated in the Code of Practice, to their investors. A couple of years ago we added to the Code of Practice a requirement for Fund Members to disclose their Diversity, Equity and Inclusion (DEI) policy to investors. Alongside this we produced some basic guidelines which we felt would be particularly useful for smaller firms, within our membership, who were not necessary up to date on best practice for DEI. AREF has its own Diversity, Equity & Inclusiveness (DEI) Policy and we expect all of our members to at least have internal policies and procedures that promote a diverse, equal opportunity and inclusive workplace and which reflect our own DEI Policy.

We feel that the FCA introducing a proportionate regulatory framework on D&I will be greatly beneficial to the real estate funds and other financial sectors. We would suggest that a future expansion of this regulatory framework to incorporate equity alongside diversity and inclusion would further enable member firms to address disparities and facilitate equitable environments where existing diversity and inclusion policies can be more successfully implemented.

Similar to other financial sectors, the real estate fund sector has improved diversity and inclusion over recent years but still has a way to go.

We support the FCA requiring firms to set a D&I strategy with targets and then having to report on these to the FCA. This will keep firms focussed on improving their diversity and inclusion. We agree that greater diversity reduces *"groupthink, supporting healthy work cultures, unlocking diverse talent and improving understanding of and provision for diverse consumer needs."*

We further support the FCA's approach to promoting D&I in the financial sector. We consider that the FCA's proposals would encourage firms not to follow a 'box-ticking' approach but one that serves its intended purpose. We also welcome

¹ The Association of Real Estate Funds represents the UK real estate funds industry and has over 50 member funds with a collective net asset value of more than £50 billion under management on behalf of their investors. The Association is committed to promoting transparency in performance measurement and fund reporting through the AREF Code of Practice, the MSCI/AREF UK Quarterly Property Funds Index and the AREF Property Fund Vision Handbook.

the FCA's focus on non-financial misconduct. We recognise that progress is being made by firms to address the barriers faced by 'diverse' individuals seeking to enter and advance within the industry and that greater effort is needed to nurture healthy, equitable and inclusive cultures.

We would ask that the FCA's rules for D&I in the financial sector leverage off existing definitions and concepts within employment law, where possible. This would assist in the transition to these new regulations and avoid ambiguity in the rules.

We have provided detailed comments on the questions included in the consultation in the appendix to this letter.

AREF is keen to engage with the FCA as it works to develop its regulatory approach to DEI and help drive necessary change in the financial services sector.

Please contact either myself (prichards@aref.org.uk) or Jacqui Bungay (jbungay@aref.org.uk), Policy Secretariat at AREF, to discuss any aspect of our response.

Yours sincerely



Paul Richards

Managing Director, The Association of Real Estate Funds

Appendix

1. To what extent do you agree that our proposals should apply on a solo entity basis?

We agree that the FCA's proposals should apply on a solo entity basis.

We consider that counting only employees who predominantly carry out activities from an establishment in the UK towards the proposed 251 employee threshold for D&I additional requirements, in principle, is appropriate. It can help ensure that reported data is not inadvertently obscured, and progress at individual firm level.

2. To what extent do you agree with our proposed proportionality framework?

We agree with the FCA's proposed proportionality framework. We support the application of a minimum standard to all Financial Services and Markets Act (FSMA) firms with a part 4A permission with the aim of reducing discrimination and misconduct and the introduction of additional D&I requirements for firms with 251 or more employees.

A key element of improving DEI in the industry is developing equitable and inclusive cultures. We consider that the FCA's proposal to embed non-financial misconduct into fitness and propriety assessments, the Conduct Rules and guidance on the Suitability Threshold Condition and to apply the rules to all in-scope firms, regardless of size, is an important step in achieving this goal.

We agree that additional requirements – that is, developing an evidenced-based D&I strategy; requiring a firm's Board to be responsible for the maintenance and oversight of the D&I strategy; setting targets to address underrepresentation; publicly disclosing targets and a firm's progress towards them annually; annually collecting and reporting to regulators data across a range of mandatory demographic characteristics, a selection of inclusion metrics and targets via a regulatory return; publicly disclosing the same information annually; and adhering to new FCA guidance on risk and governance – should only be mandated for firms with 251 or more employees. We consider that D&I requirements should be proportionate to a firm's structure and complexity.

3. Are there any divergences between our proposed regulatory framework and that of the PRA that would create practical challenges in implementation?

The FCA and PRA proposals are broadly in line with one another. While the PRA take a more prescriptive approach to setting targets, we believe the approaches are similar and thus the implementation challenges will be similar too.

4. To what extent do you agree with our definitions of the terms specified?

We agree with the FCA's proposed key defined terms – that is the definitions of Discriminatory Practices, and Senior Leadership which are broadly in line with pan-industry definitions and Diversity and inclusion employee number which is in accord with the FCA's aforementioned proposals in consultation question 1.

5. To what extent do you agree with our proposals to expand the coverage of non-financial misconduct in FIT, COCON and COND?

We agree with the FCA's proposals to expand the coverage of non-financial misconduct in FIT, COCON and COND.

We consider that individuals working in financial services should meet a basic standard of conduct and behaviour, particularly where they serve a diverse investor base. We also consider that adverse findings in respect of non-financial misconduct, such as conduct relating to D&I, has implications for an individual's honesty, integrity and reputation and for wider market confidence in the sector. Therefore, non-financial misconduct should form a part of staff fitness and propriety assessments, the Conduct Rules and the suitability criteria for firms to operate in the financial sector.

6. To what extent do you agree with our proposals on data reporting for firms with 250 or fewer employees, excluding Limited Scope SM&CR firms?

We agree with the FCA proposals on data reporting for firms with 250 or fewer employees, excluding Limited Scope SM&CR firms.

We consider requiring all FSMA firms with a Part 4A permission with 250 or fewer employees, excluding Limited Scope SM&CR firms, to report their average number of employees for the purpose of monitoring which firms are in scope of the additional D&I requirements is appropriate.

7. To what extent do you agree with our proposals on D&I strategies?

We agree with the FCA's proposals on D&I strategies.

We support requiring large firms to develop an evidence-based DEI strategy that contains the firm's DEI objectives and goals; a firm's board being responsible for the maintenance and oversight of the firm's D&I strategy; a plan for meeting those objectives and goals and measuring progress; a summary of the arrangements in place to identify and manage any obstacles to meeting the objectives and goals; and ways to ensure adequate knowledge of the DEI strategy amongst staff can help firms to take a proactive approach to advancing their DEI aims and evaluating progress.

We also note and support the FCA's intention to provide a high-level framework that gives firms the flexibility to devise strategies that most effectively deliver the outcomes the FCA wants to see, taking account of their own needs and operating environment, and we would be interested in engaging with the FCA as it works to develop this framework.

8. To what extent do you agree with our proposals on targets?

We agree with the FCA's proposals for firms setting targets and reporting their targets and progression to the FCA. However, we do not support it being mandatory for firms to publicly disclose their targets and progress towards them.

We consider that targets are imperative for any goals to be achieved whether they be financial or diversity related and we would suggest that the FCA consider mandating that the targets cover the Gender and Ethnicity demographic characteristics as a minimum but not prescribe what those targets should be.

However, we appreciate that there are different views within the industry regarding the effectiveness and practicability of targets for Board members, senior leadership and the employee population as a whole (which includes the Board and senior leadership). Some consider that targets are necessary to propel greater diversity, whereas most support flexible goals which are decided by individual firms. Additionally, some firms consider that targets encourage a 'box-ticking' attitude to improving diversity which may not consider a firm's wider context and may lead to employed individuals believing that they were selected out of tokenism, and/or the wider workforce believing this to be the case.

We understand that many firms are already setting and publicly disclosing their DEI targets. However, there may be valid reasons why firms do not wish to disclose publicly their DEI targets and their progress towards them. This could be due to the firm's global strategy or potential political and/or legal concerns based on the regions they operate in.

9. To what extent do you agree with the date of first submission and reporting frequency?

We agree with the proposed date of first submission and reporting frequency to the FCA.

We welcome the FCA's willingness to enable firms to establish the necessary processes for reporting data to the FCA and introduce a transitional regime which enables the first reporting cycle to be on a 'comply or explain' basis.

10. To what extent do you agree with the list of demographic characteristics we propose to include in our regulatory return?

We agree with the list of demographic characteristics that the FCA proposes to include in its regulatory return.

We consider that the list of demographic characteristics should be aligned with the protected characteristics set out in the Equality Act 2010, excluding pregnancy/maternity and marriage or civil partnership. We agree with the FCA that aggregated pregnancy/maternity and marriage or civil partnership data would not provide sufficient insight into the experiences of those who share this characteristic. We consider that taking a broad approach and collecting data across all the proposed demographic characteristics would not necessarily be a useful exercise and that the FCA should collect data across the areas where most firms already gather metrics, with a view to developing the scope of mandatory and voluntary data collected over time.

11. To what extent do you agree that reporting should be mandatory for some demographic characteristics and voluntary for others?

We agree that reporting should be mandatory for some demographic characteristics and voluntary for others.

We consider that making reporting mandatory for some demographic characteristics can be useful in enabling the FCA and firms to compare and benchmark industry progress, and we consider that the list of mandatory demographic characteristics could be extended at this stage to include socio-economic background, which we understand significantly intersects with ethnicity. However, we consider that the proposed list of mandatory demographic characteristics may be challenging for firms to report on, particularly firms with employee numbers closer to the 251-employee threshold and in the context of a planned reporting date of 2025 (12 months from the expected publication date of the final rules). The FCA should take an incremental approach to reporting and initially mandate data across the characteristics where most firms already gather metrics, such as age, sex or gender and ethnicity, to minimise gaps in reported data.

12. Do you think reporting should instead be mandatory for all demographic characteristics?

We do not consider that reporting should be mandatory for all demographic characteristics, however, we agree that reporting should be on the basis of the FCA in 3 categories: board, senior leadership and all employees.

We consider that the collection and monitoring of diversity data by individual firms can be important in driving improvements in DEI in the financial services sector. It can help firms to understand their starting point, identify areas for intervention and measure progress. We recognise that, in practice, reporting diversity data can be challenging as it relies on employees opting-in to share sensitive personal information which they may not feel comfortable disclosing. This challenge can be greater in smaller firms (including firms with close to the proposed 251-employee threshold) where the number of senior management staff is less and information could identify an individual. We consider that it is more appropriate to permit firms to approach data collection in a way that is sensitive to their structure.

We recognise that, in due course, firms may be able to report on a greater number of demographic characteristics. However, we consider that firms should retain a degree of flexibility and be able to consider what reports makes sense in line with their evolving DEI strategies and businesses. We do not consider mandatory reporting against all demographic characteristics – which we expect to increase and adapt over time - as the most effective way to drive DEI in financial services. We note that certain demographic characteristics, such as religion, sexual orientation and parental/carer responsibilities, are generally regarded as less visible characteristics and employees may be more reluctant to provide data on these characteristics, which creates operational and administrative complexities for firms.

We suggest that periodic thematic reviews by the FCA could be a useful tool to evaluate how the categorisation of demographic characteristics and scope of reporting requirements could be improved with time.

13. To what extent do you agree with the list of inclusion questions we propose to include in our regulatory return?

We agree with the list of inclusion questions that the FCA proposes to include in its regulatory return, however, in line with AREF's own policies, we consider that the Culture & Inclusion section should be expanded to include and highlight equity within member firms.

Data on demographic characteristics does not always provide a representation of a firm's commitment to supporting change within the industry, particularly for smaller firms with low staff turnover. In principle, we support a standardised set of inclusion questions measured on a five-point scale of 'strongly agree' to 'strongly disagree' which measures areas such as leadership, safe and speak up culture, systems and processes, employee perceptions, employee actions and structure. We consider this can serve as a useful way to track changes in culture, evidence improvements and help firms to better understand their employees and what can be done to attract and retain 'diverse' talent. We would reemphasise the importance of capturing the data on inclusion on an anonymous and voluntary basis, and would suggest separating the collation of inclusion data from the collation of diversity data, to ensure anonymity.

14. To what extent do you agree with our proposals on disclosure?

We agree with the FCA's proposals on public disclosure to a limited extent.

We consider that there are both positives and negatives with mandating public disclosures on D&I data. Through increasing transparency and facilitating comparisons between firms on D&I performance, public disclosures could heighten reputational risk for firms and prompt greater internal discussion about changes. However, in placing an emphasis on publicised data, the FCA may encourage firms to implement practices that are tokenistic and only provide impact over the short term. It also provides a misconception that firms alone can or should improve D&I in the industry. Diversity disparities in the investment industry and wider financial sector stem from deeper and more complex issues beyond the workplace, such as quality of school support or careers advice to individuals of certain demographics. Whilst focusing on firm data can facilitate internal change, it does not address the systemic issues that create or exacerbate workplace disparities and are a significant barrier to long-term impact.

15. To what extent do you agree that disclosure should be mandatory for some demographic characteristics and voluntary for others?

We agree that reporting should be mandatory for some demographic characteristics and voluntary for others, and we reiterate that we consider socio-economic background should be included in the list of mandatory demographic characteristics.

16. Do you think disclosure should instead be mandatory for all demographic characteristics?

As explained in our response to Question 12 of the consultation paper, we do not consider that disclosure should be mandatory for all demographic characteristics.

We consider that the retention of voluntary metrics is particularly important in the context of public disclosures. While an employee may support the reporting of their D&I data to the FCA, as a regulator, they may be less willing to disclose the same or similar personal data where it will be publicly accessible.

17. To what extent do you agree that a lack of D&I should be treated as a non-financial risk and addressed accordingly through a firm's governance structures?

We agree, to a limited extent, that a lack of D&I should be treated as a non-financial risk and addressed accordingly through a firm's governance structures.

We consider that for any weight to be placed on the collation and submission of D&I Data and Strategies, the consideration of it as a non-financial risk is important. Additionally, we would expect, in time, that the FCA amend its rules and guidance to require an individual within each firm to be assigned responsibility for D&I.

We would also suggest that, in the future, the FCA develop its proposals on board recruitment, succession planning and talent pipelines, which we consider could have an impactful and long-lasting effect on the industry.

18. Do you have any comments on the cost benefit analysis?

We do not have any comments.