



AFMA CONSEQUENCE MANAGEMENT STANDARD

Australian Financial Markets Association

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AFMA Consequence Management Standard

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Australian Financial Markets Association

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A Principles Based Standard for Consequence Management

This AFMA Consequence Management Standard (Standard) sets out Principles to guide AFMA Member firms in the design and implementation of a consequence management policy for their employees. Member firms are expected to reflect the Principles in the consequence management policy they apply to AFMA accredited employees in relation to Code of Conduct matters.

Member firms may have established internal policies and procedures in relation to consequence management that they apply across their global network for consistency. In such instances, whilst such member firms are expected to adopt the Principles set out in this Standard where necessary, it is expected there will be differences in implementation.

For the avoidance of doubt, this Standard does not create any enforceable rights or entitlements in favour of any individual working in the Member firms. These individuals remain covered by the relevant internal policies and procedures relating to consequence management in place in these Member firms and not by this Standard.

Monitoring and Detecting Employee Misconduct

While not part of this Standard, it is noted that for consequence management to be effective it is necessary for firms to have risk-based processes in place to monitor their employees' conduct of their responsibilities. These processes should be capable of identifying conduct that is not in accordance with the relevant financial services law, regulatory requirements or the firm's policies (incorporating its accepted industry standards).

This Standard outlines requirements for consequence management policies as they relate to the period from the time an investigation is completed and the subsequent process to determine the consequences for the employee, and some related communications and record keeping.

1. Principles

The AFMA Consequence Management Standard is centred on a set of Principles to guide the design and implementation of an effective consequence management policy. These are accompanied by guidance in Section 3 to assist in the practical application of the Principles.

CONSEQUENCE MANAGEMENT PRINCIPLES

Existence and Purpose

Principle 1

- a) *The Firm's control environment should incorporate a Consequence Management Policy. The Policy should have an objective to deal with incidents of non-compliance with the Firm's internal policies and standards, applicable law, the Firm's obligations as an entity licensed or as authorised by a government body and industry standards that are recognised by the Firm. The Policy may be a single all-inclusive policy or consist of an integrated set of measures that provide a comparable outcome, including an appropriate governance framework, supporting policy architecture and compliance monitoring processes.*
- b) *The Firm's Consequence Management Policy should state its scope in terms of the internal policies covered, applicable law and industry standards adopted by the Firm and the business areas covered.*

Approval of Policy and Implementation

Principle 2

The Firm's Consequence Management Policy should be approved by its Board, or its delegate, to ensure that the policy is appropriate to its purpose and is properly implemented.

Assessing Employee Misconduct

Principle 3

The Consequence Management Policy should require the firm to assess the severity of an incident of misconduct by an employee by referencing the full context of the situation, at a minimum including such matters as those listed in (a)-(e) below, and to determine the consequences for the employee accordingly:

- a) *Extent of the breach of company policies;*
- b) *Adverse impact on customers and market integrity;*
- c) *Adverse impact on the Firm (financial, legal and reputational harm);*
- d) *The degree of culpability of the employee adjusting for any mitigating factors; and*
- e) *The need to support a 'speak up' culture, whistle-blower programs and to promote reporting and escalation.*

Procedural Fairness

Principle 4

The Consequence Management Policy should require that process to determine the consequences are procedurally fair and is applied in a proportionate, consistent and transparent way for the employee.

Communication and Escalation

Principle 5

- a) The Consequence Management Policy should define a process to escalate and communicate an incident and its consequence(s) to internal parties (e.g. senior management).*
- b) The Consequence Management Policy should define a process to report serious compliance concerns to external parties to the extent required by regulation, law or contractual obligation.*

Record keeping

Principle 6

The Consequence Management Policy should require that, where the consequence is serious enough to warrant it, the Firm should maintain records of cases where a consequence was applied to an employee in a form that enables:

- a) Verification that consequence measures have been implemented; and*
- b) Facilitates analysis to inform the overall risk profile of the Firm.*

2. Principles and Implementation Guidance

This section provides guidance that is designed to assist firms in understanding and applying the Principles.

Existence and Purpose

Principle 1

- a) *The Firm's control environment should incorporate a Consequence Management Policy. The Policy should have an objective to deal with incidents of non-compliance with the Firm's internal policies and standards, applicable law, the Firm's obligations as an entity licensed or as authorised by a government body and industry standards that are recognised by the Firm. The Policy may be a single all-inclusive policy or consist of an integrated set of measures that provide a comparable outcome, including an appropriate governance framework, supporting policy architecture and compliance monitoring processes.*
- b) *The Firm's Consequence Management Policy should state its scope in terms of the internal policies covered, applicable law and industry standards adopted by the Firm and the business areas covered.*

Guidance

The Firm must have robust, transparent and consistent practices for managing consequences of noncompliance with its policies, as this is a critical element of good risk culture and key to ensuring that staff conduct is aligned with this. These should be articulated in the form of a Consequence Management Policy, which may exist as a specific policy or may consist of an appropriate governance framework with supporting policies and compliance monitoring processes. Note that while compliance monitoring process are mentioned as one method of implementation, firms may vary in relation to which business function(s) (e.g. Compliance, HR, Risk) that implement the policy (or parts of the policy).

Scope of policies covered

The Firm's Consequence Management Policy should set out its scope in terms of the applicable internal policies and the functions and business areas that it covers.

The Firm's relevant policies should incorporate or refer to industry codes and conduct standards that the Firm recognises and agrees to observe. For example, a large investment bank may incorporate the principles that form AFMA's Code of Conduct (AFMA Code) into its internal code and policies or it may instead directly refer to the AFMA Code as a policy that must be observed by its employees. Smaller Firms may wish to adopt the AFMA Code as an internal policy.

The scope of internal policies that are covered by the Consequence Management Policy may include (but are not limited to):

- employee manuals;
- code of conduct;
- procedures to be adopted;
- appropriate workplace behaviour; and
- employment/workplace relations.

Scope of conduct covered

Deficient technical competency and misconduct are two dimensions of unprofessional behaviour. This Consequence Management Standard is designed for Consequence Management Policies that focus on the misconduct (i.e. conduct in breach of covered policies). Other shortcomings in the employee's competent performance of their responsibilities (for example, a technical failing in administration or mismanagement of a situation) might be better addressed through general management procedures, including systems for performance management.

While this standard can only briefly consider positive consequences due to its scope, firms are encouraged to consider how recognition can be given to positive behaviours aligned with or exceeding expectations and requirements through balanced scorecards and other performance management measures.

Approval of Policy and Implementation

Principle 2

The Firm's Consequence Management Policy should be approved by its Board, or its delegate, to ensure that the policy is appropriate to its purpose and is properly implemented.

Guidance

The Board is ultimately responsible for decisions regarding the culture and values that should govern the operation of an entity, including the extent of the risks it is prepared to take to meet its objectives. Board approval of the Consequence Management Policy adds weight to its impact and introduces a high level of accountability for the management team to implement the policy in a diligent and effective manner.

The design of the Consequence Management Policy and the approach taken to its implementation should reflect the Board's decisions on culture and its calibration of acceptable risk.

It is the role of management to design and implement measures to ensure that the entity operates within the value system and risk appetite set by the Board.

The Board or its delegate, may delegate its authority in respect of consequence management to a properly qualified committee, provided this is reflected in the committee's charter, or to the Senior Officer Outside of Australia (SOOA) for a foreign ADI.

As an alternative, the Board may provide framework guidance to senior management who may then formulate the operational content of its Consequence Management Policy.

Assessing Employee Misconduct

Principle 3

The Consequence Management Policy should require the firm to assess the severity of an incident of misconduct by an employee by referencing the full context of the situation, at a minimum including such matters as those listed in (a)-(e) below, and to determine the consequences for the employee accordingly:

- a) Extent of the breach of company policies;*
- b) Adverse impact on customers and market integrity;*
- c) Adverse impact on the Firm (financial, legal and reputational harm);*
- d) The degree of culpability of the employee adjusting for any mitigating factors; and*
- e) The need to support a 'speak up' culture, whistle-blower programs and to promote reporting and escalation.*

Guidance

Assessment Factors

Principle 3 lists factors that should be considered when assessing the seriousness of a particular breach. As a guide it might also be appropriate to include consideration of the following factors:¹

- whether the matter involved a mistake, recklessness or negligence;
- whether the matter involved dishonesty or a breach of trust;
- the degree of responsibility for the breach and whether there was any provocation, persuasion or coercion by other parties;
- the adequacy of the employee appointment process (and criteria) and/or the nature of training provided by the Firm (including via a third party) having regard to the activity in question;
- the extent to which it may have reflected a culture or common practice in the work area which needs to be addressed as a systemic problem or supervisory failing;
- the employee's intention and whether it was premeditated or unintended;
- if any personal benefit was gained;
- the amount of any loss or damage caused to clients, the Firm or other parties;
- the impact on the market, including potential loss of public confidence;
- the duration of the matter;
- the actual and potential consequences of the breach; and
- efforts by the employee to report, escalate, mitigate or remedy the situation.

The above is not an exhaustive list.

¹ Adapted in part from *Handling Misconduct - A human resources practitioner's guide to the reporting and handling of suspected and determined breaches of the APS Code of Conduct* A Good Practice Guide, Australian Public Service Commission, <https://www.apsc.gov.au/chapter-6-determination-and-sanction>

Consequences

The consequences for the employee should be determined in accordance with the seriousness of the incident of misconduct and their culpability. Account should be taken of any mitigating factors, including self-reporting and the need to promote a culture of speaking up and any aggravating factors, such as an attempt to conceal the breach.

It is also reasonable for the Firm's process to take account of other pertinent factors and consideration of this should form part of the assessment process. This should include matters like the employee's degree of responsibility, experience, qualifications, training provided and support available to them in their role.

In general consequences should be scaled to be more severe for more serious matters, however, the full context of the matter and any previous matters should be considered. In practical terms this may include:

- the number, nature, severity and culpability in relation to previous matters found against the employee;
- whether the misconduct was uncharacteristic including a consideration of their length of service;
- whether the employee took steps to mitigate the risk of misconduct, such as seeking advice from their manager or another experienced employee; and
- whether the matter was self-reported or escalated by the employee and the timing and circumstances around that report. In this regard, Firms should consider the benefit of promoting a 'speak up' culture.

Firms should have a range of consequences available to respond with appropriate scale to a range of matters. Consequences might include (but are not limited to):

- informal reminders of requirements;
- remediation activities by the employee;
- additional supervision, training or professional accreditation;
- reassignment or restrictions or supervision or monitoring of activities;
- counselling, reprimands or formal verbal and written warnings;
- financial consequences including through performance management such as loss or reduction in value of a bonus, or the payment of a financial sanction;
- internal rating or promotion impacts;
- redeployment in a different role;
- dismissal (with and without notice, with and without cause);
- removal of the Firm's support for ongoing professional accreditation; and
- reporting to regulators if required

For minor matters it may be appropriate that no consequence is applied.

For the most serious matters consequences considered should include the potential for dismissal and the withdrawal of support for professional accreditation.²

² It is noted that a loss of professional accreditation can result in increased difficulties for individuals to find work within the industry in which they are qualified and experienced and so has greater potential to create hardship than dismissal. Therefore, and in alignment with ASIC's approach to Code monitoring schemes, the explicit withdrawal of support for professional accreditation should be considered a very serious sanction for use in "extreme circumstances". This approach reflects ASIC RG 269, para 145(i).

Procedural Fairness

Principle 4

The Consequence Management Policy should require that process to determine the consequences are procedurally fair and is applied in a proportionate, consistent and transparent way for the employee.

Guidance

Transparency to Employees

A successful Consequence Management Policy requires employee understanding which in turn requires transparency of the Consequence Management Policy and associated processes. Transparency is also necessary for fairness. The Firm should provide the policy to all the employees to whom it applies and ensure that it is readily available to employees on an ongoing basis. Employees should be advised of their responsibility to familiarise themselves with the policy and its operation. Firms may wish to consider a requirement for staff to receive periodic training on the Consequence Management Policy.

Procedural Fairness

The consequence management processes that flow from the Consequence Management Policy need to only include the minimum formality and time necessary to allow a proper consideration of the matter.³ This reflects the principle stated by Mason J in *Kioa v West*⁴ that ‘the expression “procedural fairness” ... conveys the notion of a flexible obligation to adopt fair procedures which are appropriate and adapted to the circumstances of the particular case’. For less serious matters or matters where the potential sanctions are more minor this means that informal arrangements can be sufficient.

Matters should be managed on a case-by-case basis. The circumstances of the matter and prior behaviour, including any other breaches, of the employee should be considered before making a determination in relation to consequences.

The consequence should be assessed and determined by suitably qualified personnel who can provide a high degree of objectivity and operational insight into the process. For example, a consequence management situation may be properly assessed by the relevant business head (or equivalent), with support from HR, compliance and risk management personnel, as appropriate. In small firms, it may be appropriate for an appropriately qualified person (including experience and impartiality) to conduct this process.

Decision makers should be made aware of the Firm’s policies that need to be respected when making consequence management assessments and determinations; for example, those concerning employee relations. While all cases should be dealt with on their own merits, decision makers should endeavour to be consistent in their treatment of the various cases dealt with under the policy.

³ Adapted from the Australian Public Service Commissioner’s Directions 2013, Section 6.6, <https://www.legislation.gov.au/Details/F2015C00944>

⁴ (1985) 159 CLR 550.

The Firm may wish to deal with low impact incidents and breaches of policies in a different way to its response to more serious matters. This may provide more efficient outcomes for some Firms, especially by managing the use of senior management time and resources. This may also signal more clearly to the employee and other affected personnel the relative seriousness of the matter being considered. This outcome can be achieved by less formal processes.

To further promote procedural fairness, the process for determining the consequence for an employee should generally:

- allow the employee an opportunity to be heard before the decision maker makes a decision on consequences that may be adverse to their interests;
- treat employees with dignity and courtesy and respect their rights; and
- involve unbiased and factual decision-making in which relevant principles are applied in a consistent manner.

Firms should endeavour to deal with matters in a timely manner, noting that decisions regarding certain consequences may be made as part of centralised processes conducted at a set time of year. For example, decisions regarding potential impacts to promotion prospects and/or financial consequences made as part of a year-end process.

Communication and Escalation

Principle 5

- a) *The Consequence Management Policy should define a process to escalate and communicate an incident and its consequence(s) to internal parties (e.g. senior management).*
- b) *The Consequence Management Policy should define a process to report serious compliance concerns to external parties to the extent required by regulation, law or contractual obligation.*

Guidance

The Consequence Management Policy should require that the employee be informed of the outcome of the consequence management process in a timely manner.

There may be a requirement to report an incident of misconduct to the appropriate regulatory or law enforcement agency. The legal requirement to report a breach to the regulator is a separate matter to the reporting of the outcome of the consequence management decision associated with that breach. The Firm must meet its obligations to report a breach as required under the law. For clarity, it is noted that nothing in the Firm's policy (or this industry standard) should interfere in this process.

An incident that presents material compliance concerns for the Firm should be brought to the attention of the senior management. This should include incidents that may reflect a systemic issue (i.e. may apply to a wider number of employees) or multiple incidents that relate to an employee who is involved in low scale incidents on a systematic basis.

The Firm's management should receive a consolidated report of actions taken under the policy for review on a regular basis, including progress in implementing consequence actions.

The Board or equivalent, or for large organisations, the relevant divisional business and risk heads, should be given a periodic summary report on the application of the Consequence Management Policy and should be informed of specific incidents that are determined to be sufficiently serious or indicative of a systemic pattern of misconduct to warrant their individual reporting.

Record keeping

Principle 6

The Consequence Management Policy should require that, where the consequence is serious enough to warrant it, the Firm should maintain records of cases where a consequence was applied to an employee in a form that enables:

- a) Verification that consequence measures have been implemented; and*
- b) Facilitates analysis to inform the overall risk profile of the Firm.*

Guidance

Where the consequence is serious enough to warrant it, the Consequence Management Policy should require the Firm to maintain a record of cases where a consequence is applied to an employee consequent to an incident involving a breach of its policies. This should record the details of the case and the consequences applied.

A central register of cases where the operating provisions of the Consequence Management Policy have been activated and consequences have been applied to employees should be maintained. This will support the consistent recording of incidents, management reporting, future analysis and compliance risk assessment at the firm level.

The Consequence Management Policy should identify the function(s) who have responsibility to ensure that proper records are kept.

The individual's employee record should enable the outcome of the consequence management process in one case to be considered as appropriate in assessing the existence or treatment of any future potential consequence management issue.