# Recording telephone conversations and electronic communications under COBS 11.8
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# *Guidelines*

## 1. Introduction

### 1.1. Status of these guidelines

These guidelines have been prepared by the Association of Private Client Investment Managers and Stockbrokers (APCIMS), the Futures and Options Association (FOA), the International Swaps and Derivatives Association (ISDA), the London Investment Banking Association (LIBA) ("the Associations"), in conjunction with Clifford Chance LLP, and are endorsed by the Association of Foreign Banks (AFB). The aim of the guidelines is to suggest considerations which firms may wish to take into account in deciding how to apply the Financial Services Authority's (FSA's) new Conduct of Business Sourcebook (COBS 11.8) provisions on recording telephone conversations and electronic communications, which come into force on 6th March 2009. The guidelines do not, however, purport to be definitive or comprehensive: nor do they alter the meaning of any relevant FSA provisions (and should not be interpreted as doing so).

Although their application may vary from firm to firm, these guidelines represent the broad consensus view of members of the Associations.

The Associations have kept the FSA informed of the content of the guidelines but have not sought formal confirmation; the guidelines do not, therefore, have any formal status with the FSA and cannot be relied upon as official industry guidance.

The guidelines are up to date as at the time of issue. Firms should, however, check whether there have been any changes to the FSA provisions to which the guidelines refer.

## 1.2. In-house policies

The material below seeks to outline the types of questions firms may find it helpful to ask themselves, in order to reach a conclusion as to the practical application of the new provisions. However, as a starting point, it is worth considering whether the introduction of the COBS 11.8 rules may actually present an opportunity for firms to sharpen up their policies on the different types of communication devices that may be used for business purposes and the recording arrangements that may apply to them. For example, just as many trading/corporate finance houses prohibit staff from using mobiles on the trading floor, a firm could have a recorded communications policy that specified, for example, that video conferencing and chat were not permitted for the purpose of "receiving client orders and the agreeing and arranging of transactions". In sharpening up its policies, a firm could make not only its staff aware of any restrictions imposed but also its customers, i.e. by indicating in terms of business that instructions from a client will only be valid if received via certain media.

With a view to making any such policy a comprehensive statement of its communication practices and recording arrangements, a firm might also wish to include material on other issues covered by these guidelines. For example:

- how, and upon what basis, a firm takes advantage of any of the COBS 11.8 exclusions and exemptions (section 2.4 of these guidelines);
- how a firm interprets the "reasonable steps" standard in the light of its own business circumstances (see section 3.1 of these guidelines);
- a statement of the capabilities of its recording systems, which can be referred to in the event of FSA requests (see section 3.2 of these guidelines); and
- the firm's policy as regards the retention and destructions of records (section 5 of these guidelines).

**It is important that, in making (and documenting) any decisions about compliance with the FSA requirements, firms take into account not just costs but the risks to the FSA's intended outcome of the rules; reducing market abuse.**

## 2. Scope of the new regime

### 2.1. Basic parameters

The basic parameters of the FSA's new recording regime are set by the following three requirements:

- COBS 11.8.1R(1): lists the activities to which the recording requirement applies to the extent they relate to the investments in COBS 11.8.1R(2);
- COBS 11.8.1R(2): lists the investments to which the recording requirement applies; and
- COBS 11.8.8R: specifies the telephone conversations and electronic communications, which are "relevant" for recording purposes (i.e. those within the scope of the recording and retention requirements in COBS 11.8.5R – see below).

In addition to these basic parameters, and in some cases depending on specific circumstances, a number of specific exclusions and exemptions apply. These are discussed in section 2.4 of these guidelines.

### 2.2. Territorial application

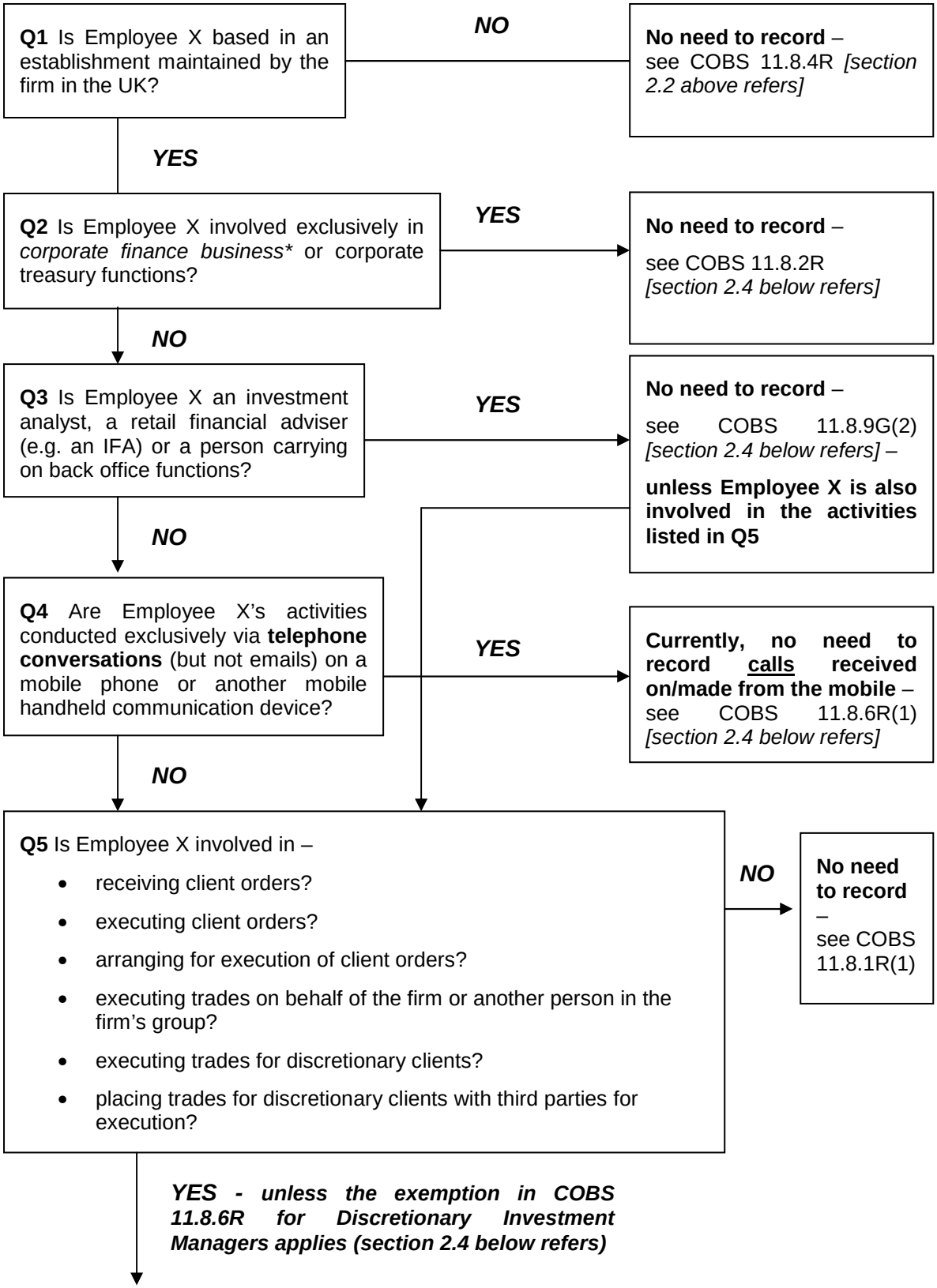
COBS 11.8.4R makes it clear that the COBS 11.8 recording requirements only apply to activities which a firm carries on <u>from</u> an establishment maintained by the firm in the UK. For this purpose, the UK is England, Wales, Scotland and Northern Ireland but <u>not</u> the Channel Islands or the Isle of Man. Where a UK firm 'passes a book' to an overseas affiliate or group member after 'London close', any telephone conversations or electronic communications, connected with orders on the book, that are made from outside the UK do not fall within the recording requirements.

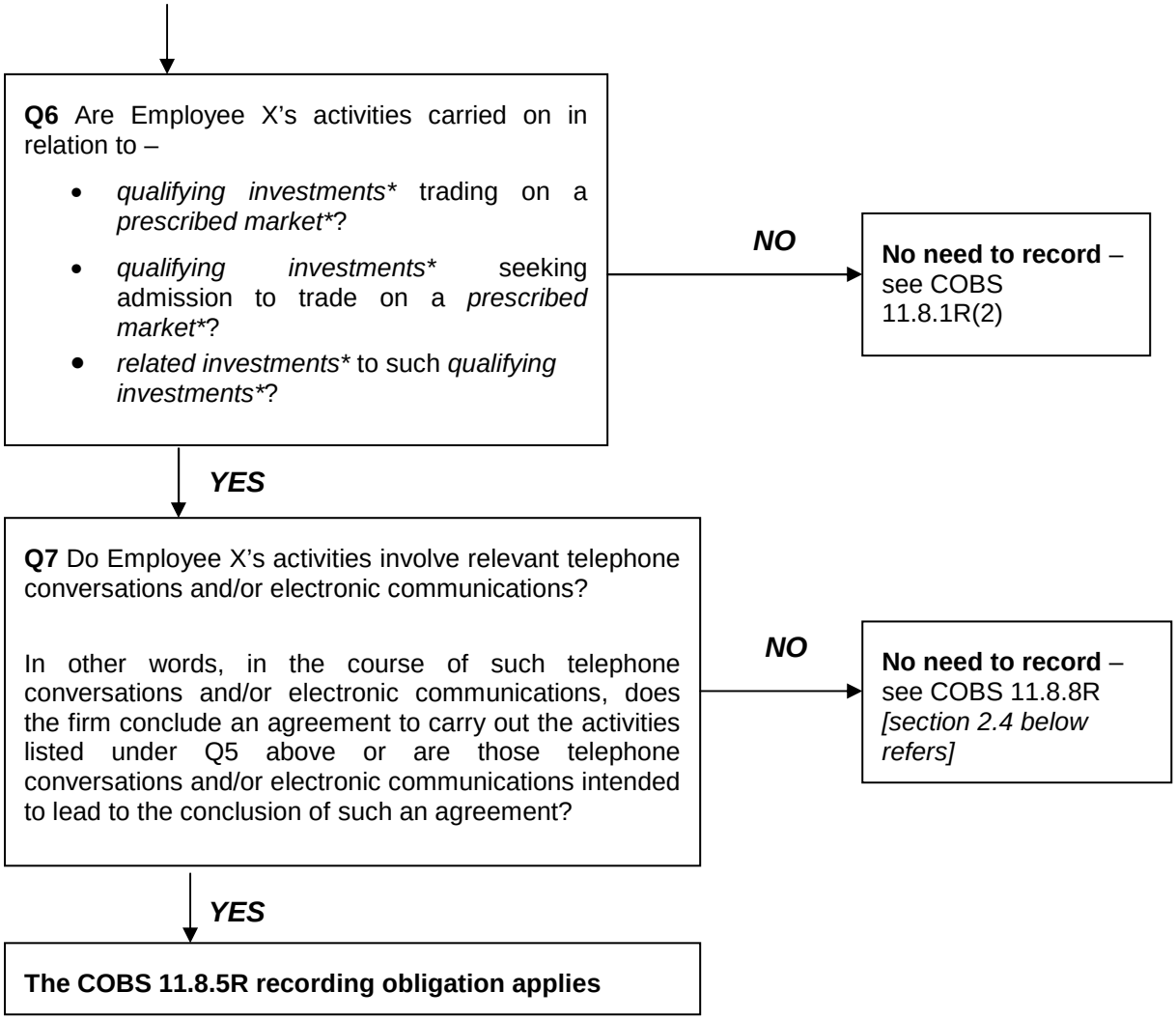
### 2.3. Practical application

While it is reasonably straightforward for a firm to determine in general terms whether its operations will be subject to the new COBS 11.8 requirements, as referred to above, it seems more difficult for firms to make this determination in respect of individual business units, functions or employees. Consequently, approaching COBS 11.8 at this level of granularity, the following table poses the question:

**IS IT NECESSARY TO RECORD THE TELEPHONE CONVERSATIONS/ELECTRONIC COMMUNICATIONS OF EMPLOYEE X?**

**A SUMMARY**






NOTES:

While COBS 11.8.8R and 11.8.9G provide further information on what conversations/communications are relevant for the purposes of the COBS 11.8.5R recording requirement (see below), in practical terms the questions above may be sufficient to determine whether a communication device which an individual uses in the course of his employment needs to be recorded,

* terms which appear in italics are defined terms in the FSA Handbook Glossary

## 2.4. Exclusions and exemptions

While the FSA's application rules focus on activities, investments and communications, as discussed above, firms need to be able to approach recording in a more practical, business-focussed way. For example, to determine: Which departments, desks or individuals need to be recorded? Which communications

media or devices need to be recorded? This section provides guidelines on how firms might do this.

### 2.4.1. Whose communications need not be recorded? - types of staff, or activity that are excepted

In COBS 11.8.9G(2), FSA states it would not ordinarily expect the conversations of:

- research analysts,
- retail financial advisers, and
- persons carrying on back-office functions,

to be captured.

In addition, those involved in:

- corporate finance business; and
- corporate treasury functions,

are excluded explicitly by COBS 11.8.2R.

Unless one of these people also has a designated trading or sales or broking role, it should not be necessary for the telephones and communication systems of these types of staff to be recorded.

The involvement of back-office staff in routine consequential actions (e.g. processing client instructions about rights issues and conversions) under pre-existing agreements does not mean that the telephones and communications systems of these types of staff need necessarily be recorded.

COBS 11.8.8R provides that recording requirements apply to conversations or communications with a client 'which conclude' an agreement and conversations and communications with professional clients and eligible counterparties that are 'carried on with a view to the conclusion of an agreement.' COBS 11.8.9G(1) provides that the requirements:

- do not apply to general conversations or communications about market conditions, and
- apply **only** to conversations that are **intended to lead to the conclusion** of an agreement.

**Telephones and communications devices used for general conversations and advice, and not used for conversations about specific deals, are not subject to a recording requirement.** Depending on the use made of them, a firm might conclude for this reason that the exception applied, for example, to conference room telephones.

Furthermore, because day-to-day communications between staff within an office are unlikely to involve the activities captured by COBS 11.8.1R, it would be reasonable for most firms to conclude that there is no need for them to record internal calls.

The exclusions point towards a conclusion that FSA rules are targeted at communications systems used by dealers, discretionary fund managers (but see section 2.4.2 below), brokers and salesmen, or people who perform these functions.

### 2.4.2. Discretionary Investment Managers

Notwithstanding that "placing orders with other entities for execution that result from decisions by the firm to deal on behalf of its client" is caught by COBS 11.8.1R(1)(f), Discretionary Investment Managers (DIMs) may be able to take advantage of exemptions from the recording requirement when they pass their trades to other firms for execution. In the new rules:

- COBS 11.8.6R(2) provides an exemption in respect of conversations/communications with a firm which the DIM reasonably believes is subject to the COBS 11.8.5R recording obligation; while
- COBS 11.8.6R(3) extends this exemption to conversations/communications with firms which are not subject to the COBS 11.8.5R recording obligation (e.g. overseas brokers) but only where such conversations/communications occur on an infrequent basis and represent a small proportion of the total telephone conversations and electronic communications made, sent or received by the discretionary investment manager to which COBS 11.8.5R apply.

As regards COBS 11.8.6R(2), it is worth noting that this exemption is enshrined within the FSA rules rather than being a matter that DIMs have to negotiate on a firm-by-firm basis with each of their brokers. This avoids the paper-chase often associated with scenarios where it may be possible for one firm to rely on another and means that a DIM would be in a position to "reasonably believe" that its

counterparty is subject to the COBS 11.8 recording requirements if that counterparty is: (i) a FSA-authorised firm operating from an establishment in the UK; and (ii) in providing services to the DIM, is undertaking the activities listed in COBS 11.8.1R(1) in respect of the investments listed in COBS 11.8.1R(2).

As regards COBS 11.8.6R(3), it is not possible to set any hard-and-fast parameters as regards how infrequent or how small-scale communications with firms not subject to the COBS 11.8.5R requirement must be, to benefit from the requirement. However, there are certain considerations which firms might take into account in determining whether they are able to make use of this exemption. For example:

- how material are the investments transacted via this route in the context of the firm's overall business, i.e. what proportion of transactions decided upon by the firm are effected via such routes? What proportion of assets under management consist of investments traded via this route?
- are trading activities conducted with such firms by means which indicate that certain forms of communication are not relevant for recording purposes? For example, if automated trading systems are used for placing orders with overseas brokers and telephone communications are limited to pursuing errors, the latter are unlikely to be caught.

In addition, while not relevant to use of the exemption per se, DIMs might wish to consider (with due regard for factors such as best execution, timeliness, cost etc) whether they can effectively bring their business with overseas brokers into the COBS 11.8.6R(2) exemption by, for example, using a UK-based intermediary (either within their group or externally) to place their trades.

It is also worth noting that, although this exemption is not available for firms which execute in-house, transactions arising from their discretionary investment management business, it is likely that the conversations/communications of individual discretionary investment managers need not be recorded if they are not in fact undertaking any of the activities in COBS 11.8.1R, e.g. because they do not receive/arrange/execute client orders and because the execution of discretionary transactions is undertaken by a central dealing desk whose conversations/communications are recorded. These individuals are the "investment managers without authority to deal" referred to in the text of both CP07/9 and PS08/1.

### 2.4.3. Which types of communication device are exempted?

COBS 11.8.6R(1) has exempted explicitly:

- conversations and communications (except emails) on mobile telephones or other handheld electronic communication devices (e.g. Blackberries).

FSA will, however, review this exemption in late 2009.

In PS08/1 FSA said that it inserted a 'reasonable steps' caveat into the requirement to record relevant telephone conversations and electronic communications in COBS 11.8.5R to reflect the reality that there may also be occasions when relevant conversations or communications take place on equipment that is not recorded because it is not routinely used for such conversations or communications. A firm need not therefore record:

- equipment that is not routinely used for the types of conversation or communication to which the rules apply.

From the FSA's discussions with trade associations, it also appears that equipment not designated for the types of conversation to which the rules apply need not be recorded. Incidental use of a non-recorded medium or device (for example, because the client chooses to do so) that has not been specifically excluded (see below), would not trigger a general recording obligation for that medium or device. However, bearing in mind the purpose of the FSA's rules – to provide evidence in market abuse cases – firms should consider whether there is anything unusual/suspicious about a client or counterparty wishing to use a non-recorded means of communication. Firms should not solicit or encourage clients to use non-recorded means of communication.

Mobile phones and handheld devices are the only types of device FSA has specifically excluded. COBS 11.8.7G and PS08/1 provide a non-exhaustive list of devices that are required to be recorded if the other conditions apply (fax, email, Bloomberg mail, video conferencing, SMS, business to business devices, chat, instant messaging). In considering whether or not devices or types of device are required to be recorded, firms will, therefore, need to consider the use for which they are designated, and may wish to consider the impact of the 'reasonable steps' provisions.

If a firm decides that certain devices will not be recorded on the basis that they will not be routinely used for the types of conversation or communication to which the rules apply, it may wish to:

- include a clear statement in any recorded communications policy that it maintains (see section 1.2) about both the types of devices/communications not subject to recording arrangements and the basis upon which the firm has concluded that recording of such devices/communications is not required; and
- consider what controls it may be appropriate to put in place to check that these devices are not being routinely used for those purposes.

## 3. Reasonable steps standards: the requirement to make recordings and the requirement to retain recordings

### 3.1. Application of a 'reasonable steps' standard

In PS08/1, FSA acknowledged that it is important for the industry to be able to interpret the 'reasonable steps' caveat in a way that is proportionate and consistent. The following guidelines deal with issues that firms might wish to consider in determining whether they have taken 'reasonable steps'.

In CP07/9 and PS08/1 the FSA stated that the implications of the new requirement were limited because many firms already recorded fixed telephone lines caught by the new requirements. Firms that already have recording systems in place may take the opportunity provided by the introduction of the recording requirement to undertake a review of their systems and consider whether existing priorities for expenditure on technology should be revised to take into account the new regulatory requirement. In light of such a review, firms may conclude that their current telephone recording systems are sufficient, at the present time, to comply with the requirement that they take 'reasonable steps'.

In PS08/1 FSA said that it inserted a 'reasonable steps' caveat to the requirement to record relevant telephone conversations and electronic communications in COBS 11.8.5 R to reflect the reality that recording systems are always likely to be fallible to some degree. Hence, where a firm takes reasonable steps to put in place and

maintain reasonably reliable recording facilities, **the fact that a technical hitch results in a recording system failing will not on its own lead to a breach of the recording requirements**. Firms should understand, however, that their "reasonable steps" may be called into question by the FSA if technical hitches occur with any degree of frequency.

Some recording systems may not be able to record relevant calls that are transferred between lines within the firm, or may be able to record electronic communications only when a daily system back-up occurs, so that, for example, emails that are deleted intra-day would not be recorded. A firm may conclude that it would be reasonable not to install system changes to address such gaps because the cost of doing so would not be proportionate to the additional relevant communications that would be captured. If a firm comes to such a conclusion, it should be aware that FSA will expect it to have a coherent explanation of how the costs outweigh the potential risks and the FSA may ask the firm to justify its decision by reference to the stated objectives of the FSA's rules: to provide evidence in market abuse cases.

In PS08/1 FSA said that its general record-keeping standard applies, requiring tapes not to be manipulated or altered. This means that COBS 11.8 does not create higher standards or expectations than apply to other record-keeping requirements, and that **firms need not, for example, where the firm's recording system is reasonably reliable, maintain duplicate copies of telephone and electronic communication recordings**. FSA said that it **does not expect firms to put in place expensive security arrangements, but rather to implement appropriate systems and controls to monitor the integrity of recordings**.

In PS08/1 FSA acknowledged that the cost of installing recording arrangements at disaster recovery sites maintained for business continuity purposes could be significant. FSA said that it may well be reasonable for a firm to decide not to install recording arrangements on cost grounds. It appears, therefore, that cost is a valid reason for firms not to have systems to enable recording at disaster recovery sites. It may be sufficient to satisfy the reasonable steps standard that the firm has plans to resume recording in the medium term.

When installing new systems, or upgrading existing systems, and taking into account technological advances, firms may wish to consider whether decisions previously made on what would comprise 'reasonable steps' should be revised.

A firm may also conclude, if it has reasonable confidence in the reliability of front-line recording arrangements, that it need not maintain back-up or duplicate recording systems.

Examples of factors firms might consider in making their own assessment of the robustness of their recording arrangements are: the specific characteristics of the recording system; the likelihood of a system failure; the ease and timeliness of rectification; the firm's internal control framework; its arrangements for testing the reliability of its recording and retrieval systems, and the arrangements for checking the coverage of recorded lines. If a firm regularly retrieves recordings for its own purposes, this activity in itself could be considered as adequate testing/monitoring of the integrity of recording systems.

### 3.2. 'Reasonable steps' – "readily accessible"

COBS 11.8.10R requires firms to record telephone conversations and electronic communications so that they are "readily accessible" to the FSA. While the FSA sets no technical standards for accessibility (e.g. as regards the use of voice recognition or word search facilities), it does indicate that it would expect firms' search facilities to support "a reasonable interpretation of readily accessible".

Given the wide range of business types that will be covered by the new COBS 11.8 rules, the term "readily accessible" will itself bear a wide range of interpretations mirroring the relative sophistication and capacity of the recording solutions adopted by different firms. So, for example, the recording arrangements of a market maker/institutional broker which has frequent recourse to recording for both in-house (i.e. to resolve trading disputes/errors) and regulatory purposes (i.e. calls for data from the FSA, overseas regulators and UK/overseas exchanges) may be much more comprehensive than those of a small retail broker which has never previously had a commercial use for recording and which has received few (if any) data requests from the FSA in the past. In considering the degree of sophistication which its recording / search facilities need to attain, a firm might wish to ask the following questions:

- Does the firm already record telephone conversations and electronic communications?

- If yes, what use has been made of such recordings in the past – primarily commercial or primarily regulatory?
- If no, will the firm be instituting recording arrangements purely to comply with regulatory requirements or can it foresee commercial uses as well?
- If recording is driven primarily by regulatory requirements, how frequently has the firm received FSA data requests in the past? Was it able to meet such requests – readily or with difficulty?

In PS08/1, FSA said that it will usually make requests for recorded information in dialogue with a firm. FSA has also, in discussions with trade associations and (in relation to requests to firms to keep recordings for longer than the 6-month minimum period) in Market Watch 28, indicated that it will:

- "…continue to use our best efforts to identify relevant material as quickly as possible, and to focus the scope of our requests so that they are as targeted as possible and are proportionate; and
- "…seek to discuss with relevant firms how best to try and identify the records that are likely to be of interest to us, and agree the practicalities of obtaining information from their systems e.g. in terms of timescales for production, format etc."

In respect of timescales for production, in the absence of any prescriptive rules or guidance, it is likely that firms may be allowed a certain amount of flexibility as long as it is considered 'reasonable'. As a starting point, the FSA indicated previously (pre-MiFID COB 3.7.5G) that, in respect of a financial promotion, "a record would be "readily accessible" if it were available for inspection within 48 hours of the request being made." There is also a read across from the current MCOB 2.8.3G, which states that "a record would be 'readily accessible' if it were available for inspection within two business days of the request being received."

The FSA has also indicated in discussions with the trade associations that:

- it will try to tailor its requests for copies of recordings to the characteristics of a firm's systems in a way that minimises the cost to the firm of retrieving and screening the recordings by seeking to formulate its requests to reflect the way in which a firms' systems are structured; and

- the nature of any data request it makes will be partly contingent upon how firms store their data and that, although it will have certain base expectations about what can be readily identified (i.e. recording made on a particular date or in relation to a particular line), its expectations would also depend upon the nature and sophistication of a firm's business.

Given the above, if firms have any concerns in respect of requests for information, they should make these clear to the FSA **immediately** so as to avoid any delays in processing such requests. In order to facilitate such discussions, firms might wish to assess, at an early stage, the capabilities and limitations of their systems in respect of retrieval.

As noted above, smaller firms putting recording systems in place for the first time, may consider, when determining the type of system to install, the nature of their business/client base, their commercial use for recordings and the level of previous data requests from the FSA. Firms need to think clearly about how they are able to meet a potential request as well as about the historic level of requests. Such a firm may come to the conclusion, based on these considerations, that a very simple system providing basic search facilities is the optimum solution given the costs involved. Obviously, the relative sophistication of firms' recording and search facilities will have a direct bearing on the ease with which FSA data requests can be met and the consequent costs and resources consumed in doing so. Hence, while large volume trading houses may opt for sophisticated systems that allow recordings to be readily and frequently searched on multi-parameter bases, smaller firms may decide that they would rather put more man-hours into fulfilling data requests as and when they are received, than install state-of-the-art systems that are rarely called upon.

Firms should also have a clear understanding of what their recording systems can actually do. In the event of receiving a data request from the FSA, it will be useful for the firm to have already available, for provision to the FSA, certain information about the way its recording arrangements operate as this will enable the FSA to consider whether it can shape its request accordingly. So, firms might wish to consider having a statement of the capabilities of their recording systems available for such eventualities covering, for example, the make and capacity of recording systems, the format in which data are recorded (e.g. tapes, CD-Roms), the search parameters

used by recording systems, the time taken to process information, the format in which selected data will be delivered to the FSA, and whether material provided to the FSA is likely to be wider than the scope of the FSA's request (i.e. whether it is possible for records that are not within the scope of the FSA's request to be excluded and, if so, what this would involve for the firm in terms of resources).

The FSA has stated in PS07/18 that they "do not require firms to search the tapes themselves" and firms with less sophisticated recording systems may not, in practice, be able to search recordings to identify the records that are of specific interest to FSA.

Other firms may need to be able to review recordings before providing them to FSA, for example to identify which parts of the recording are not covered by the FSA's request (and, taking account of associated client confidentiality and data protection obligations, to avoid gratuitously giving FSA information about other clients/counterparties who are not covered by FSA's request) or may be privileged and therefore protected items under section 413 of the Financial Services and Markets Act 2000 (FSMA).

In some cases, firms may need to carry out such a review to comply with the terms of the FSA's request (e.g. to exclude sensitive personal data or price sensitive information). Firms should not, however, otherwise "vet" information requested by the FSA.

### 3.3. Monitoring

The FSA has stated, in discussions with trade associations, that a firm is not under any obligation to monitor the communications that it records in compliance with COBS 11.8.[1]

1 Firms should be aware that although there is no obligation to listen to the recordings to seek out suspicious transactions, the FSA has discussed, in Market Watch 30, the monitoring of communications and has stated that it regards such monitoring as amongst industry good practices on the handling of rumours.

## 4. Third party access to recordings

### 4.1. Requests for recordings from other regulatory authorities

The fact that FSA rules require firms to maintain recordings may make it more likely that a firm receives requests for recorded information from other regulators, either in the UK or overseas, which are not related to the purposes (investigation and detection of market abuse) for which FSA has framed COBS 11.8; in these cases the requesting authority may not be as sensitive as FSA to the need to frame requests specifically in the context of what firms' systems are able to provide.

It is for firms to judge how to respond to such requests in the light of their obligations to the authority concerned and to their clients, but, bearing in mind that FSA introduced COBS 11.8 specifically for the purposes of investigating and detecting market abuse, and not for other purposes, it is important to note that FSA has procedures for processing requests for information on other regulators' behalf.

Under section 169 of the Financial Services and Markets Act (FSMA), the FSA may use its powers to require information under section 165 FSMA at the request of an overseas regulator. In deciding whether to exercise this power, the FSA may take into account factors set out in section 169(4) FSMA, unless it is required to do so to satisfy an EU obligation. Further information is set out in chapter 3 of the FSA's Enforcement Guide. Where a firm receives a request for information direct from an EU or third country regulator, it could, if it has no direct relationship, consider asking the regulator to direct its request through the FSA.

### 4.2. Litigation

Traditionally, communications have been recorded by firms to provide evidence of trades, and the terms on which they have been entered into, in the event of a dispute. Firms that do not already do so may wish to use the recordings required under COBS 11.8, for this additional purpose. Records of telephone conversations and electronic communications are likely to be disclosable in the event of litigation. In respect of both civil and criminal proceedings a duty to preserve documents can arise when litigation is first in contemplation. Therefore, firms should consider what systems and controls they need to put in place to preserve recordings relevant to

potential litigation, including making provision for any record destruction policy to be suspended in respect of relevant recordings.

### 4.3. Others

Whilst, under section 348 of FSMA, the FSA has a primary obligation to keep information provided by firms confidential, this obligation is subject to exceptions, sometimes called 'gateways'. There are legislative restrictions on the use of these gateways, but subject to those restrictions, it is possible that recordings provided to the FSA may be made available to other persons, for example, the FOS, HM Revenue and Customs, the competition authorities and overseas authorities. Firms should, therefore, be aware that information provided to the FSA may give rise to queries from other authorities.

## 5. Retention

COBS 11.8.10R requires firms to maintain recordings for “at least 6 months”. FSA has also published an article in Market Watch 28, in which it sets out the approach that it proposes to adopt when requesting firms to retain recordings for longer than 6 months. FSA would rely on Principle 11 (cooperation by firms with FSA) when asking firms to retain recordings for longer than 6 months.

Where a firm maintains a recorded communications policy (as per section 1.2), it may wish to include formal record retention arrangements including a clearly defined destruction policy. In the absence of a specific request from the FSA to retain certain recordings, it is for firms to determine whether to retain records beyond the 6 month regulatory minimum. In practice, firms may in a variety of other circumstances maintain recordings for longer than 6 months on their own initiative. Under Principle 11, it is possible that FSA may also seek access to such recordings when the firm still has them, even though the firm is not required to maintain them under COBS11.8. Firms may wish to consider whether their general policy, in the light of the advantages, risks and costs concerned, should be to retain recordings for the minimum 6 month period, or for longer periods. In addition, whilst retaining records may assist in commercial disputes e.g. a disagreement arising upon settlement of a twelve month contract, this is balanced by the Data Protection Principle that personal data should not be kept for longer than is necessary for the purpose for which it is obtained.

Whatever the retention period determined by the firm, as discussed above, it is important that firms follow any documented destruction policy. In addition, where a firm has a destruction policy, it should include effective communication channels so that routine destruction may be suspended if necessary. For example, when the possibility of litigation arises a firm must secure all records likely to be relevant, which may well include suspending the routine destruction of certain records.

## 6. Outsourcing

SYSC 8.1.5R(3)[2] provides that, "without prejudice to the status of any other function", the outsourcing of "the recording and retention of relevant telephone conversations or electronic communications subject to COBS 11.8" to third-party service providers "will not be considered as critical" for the purpose of the outsourcing provisions in SYSC 8. Hence, the conditions relating to outsourcing in SYSC 8.1.8R will not apply to such outsourcing, although firms should still have regard to the provisions of SYSC 8.1.3G

## 7. Data protection

Firms should consider their obligations under the Data Protection Act 1998 (the "DPA"). The DPA covers both automatically processed data and material that forms part of a relevant filing system. Information that is processed by systems that record electronic communications, such as voice activated telephone recording systems, will usually be 'data' covered by the DPA as the information will be processed by 'equipment operating automatically in response to instructions given for that purpose'. The provisions of the DPA apply only to 'personal data', being data that relate to a living individual who can be identified from those data or from those data and other information that is in the possession of, or is likely to come into the possession of, the data controller. For firms that deal only with corporate clients much of the data they receive will not be 'personal data'. However, firms should consider whether employees of the firm are likely to obtain personal data about individual traders at the clients during the course of their recorded

[2] Comes into effect on 6 March 2009

conversations. At some firms, some of the personal data they receive may be sensitive personal data[3].

Principle 1 of the Data Protection Principles requires personal data to be processed fairly and lawfully and, in particular, that it should not be processed unless: (a) at least one of the conditions in Schedule 2 of the DPA is met; and (b) in the case of sensitive personal data, at least one of the conditions in Schedule 3 of the DPA is met.

To the extent the communications are recorded and provided to the FSA in accordance with COBS 11.8, the processing of the personal data will be "necessary for compliance with a legal obligation to which the data controller is subject", one of the conditions in Schedule 2 of the DPA.

To the extent recordings may be processed for purposes other than compliance with FSA requirements, the firm will need to consider under which other conditions in Schedule 2 of the DPA the data may be processed.

The recordings will not involve the deliberate processing of sensitive data. There is no obviously applicable condition in Schedule 3 of the DPA. The firm will already be processing sensitive personal data in, for example, emails and voicemail messages just by sending and receiving them so the requirements in COBS 11.8 do not alter the existing issue of whether a firm is processing sensitive personal data fairly and lawfully. In the circumstances, the Information Commission is unlikely to object to this, provided that the firm:

- discourages employees from including sensitive personal data in telephone conversations and electronic communications except where essential for business purposes; and
- promptly deletes or disregards any sensitive data that it identifies during the course of reviewing recorded communications (save to the extent that the personal data is sensitive data because it is information about the commission or alleged commission of criminal offence the recording of which is intended to be covered by COBS 11.8).

[3] Sensitive personal data means personal data consisting of information as to race or ethnic origin, political opinions, religious beliefs or other beliefs of a similar nature, membership of a trade union, physical or mental health or condition, sexual life, commission or alleged commission of a criminal offence or proceedings for any offence committed or alleged to have been committed, the disposal of such proceedings or the sentence of any court in such proceedings.

Under the DPA[4], subject to limited exceptions, a firm will be obliged to inform individuals that it is processing personal data relating to them, if it can identify them. In many instances it will be self-evident to the participants to a communication that it will be recorded; for example, individuals working in the financial services industry should be aware of the requirements of COBS 11.8. Methods firms may use to inform persons that their communications will be recorded will vary depending upon the nature of their clients and how they communicate with them but could include one or more of:

- including information about the recording of communications in employment contracts and client agreements;
- including a statement in email disclaimers, on websites and in marketing materials;
- where reasonably practicable, using recorded messages on telephone systems;
- requiring employees, when 'cold-calling' potential clients, to inform them that the calls are recorded; or
- making clear to employees that they are not required to keep secret the existence of, or reasons for, recordings and generally encouraging employees to tell callers who may not be aware that calls are recorded.

When considering what method to use firms may wish to consider the guidance published by the Information Commissioner[5].

Firms should also consider the possibility that the recordings will involve the collection of personal data relating to individuals who are not party to the communications (i.e., persons referred to in calls or messages). In principle, where it can identify such an individual, the firm will be obliged to inform them that it is processing their personal data. However, as the firm has not obtained the data directly from the individual, it may be able to rely on the exceptions in the DPA[6] that apply where data is not collected directly from the data subject. These are: (a) that to provide information would involve disproportionate effort; or (b) that the recording of the information is necessary for

4 Under the Principle 1 of the Data Protection Principles, as interpreted in Part II of Schedule 1 of the DPA

5 See paragraph 3.2.5 of the Employment Practices Code (http://www.ico.gov.uk/upload/documents/library/data_protection/detailed_specialist_guides/employment_practices_code001.pdf) and paragraph 3.2.5 of the Supplementary Guidance (http://www.ico.gov.uk/upload/documents/library/data_protection/detailed_specialist_guides/employment_practice_code_-_supplementary_guidance.pdf)

6 Paragraph 3 of Part II of Schedule 1 of the DPA

compliance with any legal obligation. To rely on exemption (a) the firm must make a written record of its reasons for concluding that to inform would involve disproportionate effort[7].

Firms may also need to consider what policies and procedures should be put in place to comply with the other Data Protection Principles. In particular, when putting in place or reviewing, recording systems firms may wish to consider the following Data Protection Principles:

2. Personal data shall be obtained only for one or more specified and lawful purposes, and shall not be further processed in any manner incompatible with that purpose or those purposes.
5. Personal data processed for any purpose or purposes shall not be kept for longer than is necessary for that purpose or those purposes.
7. Appropriate technical and organisational measures shall be taken against unauthorised or unlawful processing of personal data and against accidental loss or destruction of, or damage to, personal data.
8. Personal data shall not be transferred to a country or territory outside the European Economic Area unless that country or territory ensures an adequate level of protection for the rights and freedoms of data subjects in relation to the processing of personal data, except where one of various specified conditions is met.

Firms may also wish to consider:

(i) how they will deal with a request by an individual for any information held by the firm that constitutes his or her personal data under section 7 of the DPA; and

(ii) whether they are required to notify the Information Commissioner that the purpose for which data is being processed has been changed. The Information Commissioner does not generally regard compliance obligations as a separate purpose requiring identification in a notification as it views them as ancillary to the purposes covering the underlying regulated activities.

In addition, in the UK, the monitoring of telephone conversations and electronic communications is regulated by the Regulation of Investigatory Powers Act 2000

[7] The Data Protection (Conditions under Paragraph 3 of Part II of Schedule 1) Order 2000

("RIPA") and the Telecommunications (Lawful Business Practice) (Interception of Communications) Regulations 2000 (the "LBP Regulations").

It is arguable that the storage of communications, and the subsequent provision of this information to a third party after it has been collected, is not 'interception' and is therefore not covered by RIPA. The Information Commissioner has expressed this view in respect of emails. In any event, by putting in place procedures to comply with the requirements of the DPA, firms will usually also comply with the exemption provided by the LBP Regulations.

## 8. International considerations

These guidelines discuss the position in the UK. If a firm provides cross-border services and therefore communicates with clients outside the UK, the data protection and privacy laws in the country of residence of those clients may apply. Firms that introduce new recording systems to comply with COBS 11.8 may want to consider whether they need to obtain specific advice on the data protection and privacy laws in countries in which they do business.

In addition, where a UK firm is owned by, or is a branch of, an EU or third country credit institution or investment firm, the laws and regulations applying to the parent company or head office will be different from those in the UK. Even if these laws do not have extra-territorial effect, discussions may still be needed with the parent/head office - particularly if there are global, group-wide policies and procedures - to explain the new UK recording requirements and raise any concerns.