Financial Conduct Authority

Discussion Paper DP14/1

Recovering the costs of administering the regulatory gateway through application fees

June 2014

Contents

We are asking for comments on this Discussion Paper by 22 August 2014.

You can send them to us using the form on our website at:
www.fca.org.uk/your-fca/documents/discussion-papers/dp14-01-response-form.

Or in writing to:

David Cheesman
Finance Division – Fees Policy
Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Telephone: 020 7066 5406
Email: dp14-01@fca.org.uk

We make all responses to formal consultation available for public inspection unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.

Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

You can download this Consultation Paper from our website: www.fca.org.uk.

Abbreviations used in this paper

AP	Approved person
AR	Appointed representative
CIC	Change in control
CP	Consultation paper
DP	Discussion paper
FCA	Financial Conduct Authority
FSA	Financial Services Authority
FSMA	Financial Services and Markets Act 2000
PRA	Prudential Regulation Authority
VoP	Variation of Permission

1. Overview

Introduction

1.1 This discussion paper (DP) by the Financial Conduct Authority (FCA) invites views on how we should recover from firms the costs of administering the regulatory gateway.

1.2 Our current structure of application fees was set by the Financial Services Authority (FSA), whose functions have, since 1 April 2013, been distributed between the FCA and the Prudential Regulation Authority (PRA). All authorised firms are regulated on conduct matters by the FCA but the PRA is responsible for the prudential regulation of banks, building societies, credit unions, insurers and major investment firms. Firms applying to be regulated by both bodies, known as 'dual-regulated' firms, currently pay a single application fee, which is split equally between the FCA and the PRA. Since 2001/02, when our fees structure was introduced, our systems and procedures have developed, and the FCA has been given a new statutory duty to promote effective competition in the interests of consumers when pursuing its other objectives of consumer protection and market integrity. A year after the establishment of the FCA and the PRA as the FSA's successor bodies, we believe it is the right moment to take stock of how we recover the costs of processing applications for authorisation.

1.3 This DP sets out some options for discussion. In the light of the comments we receive, we expect to publish proposals for consultation in October 2014, for implementation from 1 April 2015.

1.4 The PRA also intends to address the issue of application fees in its consultation paper (CP) on fees in October, and is engaging with our review.

Who does this document affect?

1.5 This document affects all firms already regulated by the FCA and the PRA, and any firm considering undertaking financial services business from 1 April 2015 onwards.

1.6 We are restricting the discussion in the DP to the 18,500 firms in the FCA's 'A' fee-blocks, but when we prepare our proposals for consultation in October, we will consider whether there are implications for the way we charge other types of firm such as payment services providers, electronic money issuers, issuers and sponsors of securities and mutual societies.

1.7 We are not addressing consumer credit application fees in this review. Consumer credit is a new regulatory responsibility for the FCA and the charging structure for applications was introduced on 1 April 2014. The firms formerly licensed by the Office of Fair Trading will be deciding, between April 2014 and March 2016, whether to apply for FCA authorisation. To maintain continuity, we are not planning to adjust the charging structure for consumer credit applications at this stage.

Is this of interest to consumers?

1.8 As firms will in the long-run recover their costs from their customers, retail consumers and consumer groups may be interested in the discussion.

Equality and diversity implications

1.9 Our initial equality impact assessment of application fees has concluded that 'straightforward' application fees are relevant to the equalities agenda because they are most commonly paid by sole traders, among whom we believe groups with protected characteristics may be disproportionately represented. Reducing or subdividing the straightforward fees would mitigate the risk of treating people with protected characteristics less favourably than other groups, and we have kept this in mind in preparing this DP. We will carry out a new equality impact assessment in the light of the comments received when we formulate our proposals for consultation in October.

Context

1.10 The FSA's original policy has not changed since 2000, and has not been reviewed since 2006/07. The rates have not changed since 2001, apart from a reduction in the 'straightforward' fees paid by the smallest firms in 2004. Consequently, the fees have gone down in real terms – by about 36% – since they have not been adjusted for inflation.

1.11 Since our gateway controls the entry of all firms to the market, our authorisations policies and processes are integral to each of the statutory objectives set for the FCA when it was established last year – consumer protection, market integrity and competition. In this paper, we are looking only at how we recover the costs of the gateway, and this is most relevant to our competition duty to promote effective competition in the interests of consumers when taking actions to pursue our consumer protection and intergrity objectives. We need to ensure that cost recovery is structured to avoid unjustified barriers to entry into or expansion within the markets we regulate.

1.12 We accordingly believe the time is right to review our policy on recovering the costs of the gateway. Rather than proceeding directly to consultation, we would first like to engage our stakeholders in the debate by issuing this DP.

Summary of the discussion

1.13 This DP covers the following topics:

- Operating the gateway.
- Distributing the recovery of authorisation costs between different fee-payers.
- Suggestions for revising application fees.

1.14 The DP focuses only on application fees. We are not considering the other regulatory and non-regulatory considerations that might affect a firm's decision to enter a market, such as the authorisation process itself and the ongoing costs of compliance.

Next steps

1.15 This DP presents options for discussion. We are not making proposals for action at this stage, but the comments we receive will help us develop our policy, so we are keen to receive as wide a range of opinion as possible. Please send us your views by 22 August 2014, using the online response form on our website, or by writing to us at the address or email account on page 2. We may share the responses with the PRA, unless you specifically ask us not to.

1.16 We will issue proposals for consultation in October, with a view to introducing the new structure from 1 April 2015.

2. Operating the gateway

2.1 This chapter summarises our role as gatekeeper, the processes involved, our current charges and our costs.

Role of the gatekeeper

2.2 The overall aim of authorisation, both for the FCA and the PRA, is summarised in the guide to *The FCA's approach to advancing its objectives* (July 2013). It is to 'ensure that firms and individuals who enter the financial industry meet our standards and are equipped to operate in the market.' Ensuring the quality of entrants to the market helps to protect consumers, while businesses that are already established benefit from operating in a market that is generally regarded as credible.

2.3 A firm seeking to enter the market must satisfy two requirements before we consider its case. First, it completes an application using the form specified by us, then it pays us the appropriate fee. Since receipt of the fee is the trigger that initiates the authorisation process, it is important that it is set at a level which does not represent an unreasonable barrier to market entry.

2.4 Our fee will, however, only be one of a number of charges a new firm has to meet when setting itself up. Depending upon its size and complexity, a firm may need to engage a wide range of professional advisers long before it needs to consider applying for authorisation. It may have to pay legal, accountancy and other professional fees, incorporate itself as a legal entity, take out appropriate insurance, engage staff, rent accommodation and equipment, provide appropriate financial and capital cover, etc. The most complex firms may submit their applications through specialist compliance consultants whose fees might amount to considerably more than our own charges. In its review of barriers to entry, expansion and exit in retail banking, published in 2010, the Office of Fair Trading concluded that our fee of £25,000 for authorisation as a bank was 'comparatively small' and they had received no evidence that the cost had deterred entry.[1] If our application fees do have any material influence on business planning, we believe they are most likely to affect the smallest and simplest firms, which have few additional costs. For a self-employed sole trader, operating from their own home and completing their application personally, our fee of £1,500 may well be the most significant single financial outlay in the set-up process.

2.5 In addition to cash expenditure, complying with our regulatory requirements carries its own resource implications. Setting the threshold for entry at the optimum level is a matter of judgement. We have to maintain appropriate standards without stifling innovation or competition. Our processes are designed to assess whether applicants understand our conduct and prudential requirements, including risk management, product design and achieving good customer outcomes through corporate culture; and, how seriously they take their obligations. We have to keep our processes proportionate so that they do not in themselves become barriers to entry.

1 Office of Fair Trading, *Review of barriers to entry, expansion and exit in retail banking* (OFT1282, November 2010), paragraph 5.28.

2.6 We have been investing both in maintaining high quality decision making and in ensuring we are continually improving the efficiency of our processes. This is intended to help us deal efficiently with lower risk applications and focus our resources on the higher risk applications that pose the greatest threat to consumers and the UK financial services market place. We expect to continue this programme of change, with perhaps the biggest change being our investment in a new case management system, to help facilitate better quality applications and case handling.

Administrative processes

2.7 The main administrative processes involved in FCA authorisations are:

- Applications for authorisation by firms wishing to enter the market.
- Variations of permission (VoPs) by firms that are already authorised and wish to extend or reduce the range of activities they are permitted to undertake.
- 'Passporting' applications and VoPs by the UK branches of firms that are based in other countries of the European Economic Area, so are primarily regulated by their home regulator.
- Applications for individuals to be recognised as 'approved persons' (APs) – for example, because they are being appointed to significant influence functions within firms or are providing intermediary services to retail customers.
- Cancellations – where firms wish to leave the market, often because they are in liquidation.
- Applications for firms to adopt sensitive business names.
- Waivers – where a firms applies to waive or modify compliance with a particular rule.
- CRR Permissions – where a CRD IV (Capital Requirements Directive) firm is applying for Permission to use the relevant discretion under the Capital Requirements Regulations (CRR).
- Changes in control (CiCs).

Charges for application

2.8 In practice, we only recover our costs from a narrow range of processes – applications for authorisation and increased permissions from UK firms, and changes in control when we anticipate our costs going above £50,000. We do not charge for the following:

- The Financial Services and Markets Act (FSMA) prevents us from charging for applications or VoPs by branches of EEA firms passporting into the UK – Schedule 1ZA, Part 1, paragraph 24(a).
- We do not make direct charges for the administrative actions we undertake when regulating firms. We believe that the costs of such interactions should be covered through firms' periodic fees to promote timely compliance with their obligations. For example, ad hoc charges might encourage some firms to defer applications to reduce their range of

permitted activities or cancel their authorisation, notifications of changes in name or legal status, requests for waivers, etc. We make an exception where we anticipate the costs of dealing with a change of control will go above £50,000. We consider it reasonable for the individual firm to bear the costs in these circumstances.

- Similarly, we do not charge for applications to become approved persons (APs) under section 59 of FSMA. In its first consultation paper on fees in June 2000 (CP56 - *The FSA's post-N2 fee-raising arrangements*), the FSA stated that FSMA prevented this. The FCA's view is that paragraph 24(b) of Schedule 1ZA to FSMA only prohibits the making of a rule requiring a fee to be paid by an approved person after they have been approved, but does not prohibit making a rule allowing us to charge a fee for the processing of an application for approval to perform a controlled function. However, we believe charging a fee to process approved person applications might not achieve the best policy outcome for the following reasons. Since APs are employees of firms, a fee for the processing of an application would in effect represent a charge on jobs. When we carried out our equality impact assessment (EIA) of periodic fees in 2011, we concluded that this might be interpreted as a barrier in the way of the recruitment or career development of people wishing to work part-time or job-share (reported in CP11/21 – *Regulatory fees and levies: proposals for 2012/13*, October 2011). We will review our EIA in the autumn, but we have decided that we should continue to treat applications for AP status as administrative interactions covered by periodic fees, and so we are not raising it as an issue for discussion at this stage.

2.9 Since it is not practical to attempt to recover the exact costs of processing each application, we base our charges on a matrix of complexity categories. These indicate the aggregate level of resources we anticipate it will take to determine the applications. The fee is paid for making the application. There are no refunds if a firm's application is not successful.

2.10 The structure of complexity categories was proposed in the FSA's first consultation paper on fees in June 2000 (CP56 - *The FSA's post-N2 fee-raising arrangements*). The rates were confirmed by CP79 in December 2000 for implementation from 2001 (*Feedback statement to CP56 and second Consultation paper on the FSA's post-N2 fee-raising arrangements*).

2.11 The only change since then was in 2004/05, when the straightforward fee was reduced from £2,000 to £1,500. The FSA explained that the opportunity for a reduction had arisen because streamlined application packs had been introduced for small firms, sole traders and straightforward change of entity applications. These packs simplified the application processes, reducing costs both for the FSA and firms themselves (CP04/02, *Fees and fees policy 2004/05*, January 2004).

2.12 CP56 had proposed that the FSA should review the application fees each year. This implied regular changes to the rates, but there has in practice been stability, apart from the reduction in straightforward fees in 2004.

2.13 Our current application fees and complexity categories are set out in Table 2.1. VoP fees are 50% of the appropriate application fee, except where it involves movement within a fee-block, when the charge is £250. There is no charge for VoPs to reduce the number of permissions, nor for seeking to exit the market.

Table 2.1: Current application fees and complexity categories

Category	Activities	Fee
Straightforward	Friendly Societies, firms bidding in emissions auctions, financial intermediaries (investment advisors, dealers or brokers, corporate finance advisers, home finance advisers or arrangers, general insurance intermediaries).	£1,500
Moderately complex	Home finance providers and administrators, insurance special project vehicles, managing agents at Lloyd's, portfolio managers, managers and depositaries of investment funds, operators of collective investment schemes or pension schemes, firms dealing as principal.	£5,000
Complex	Deposit acceptors, dormant fund operators, general and life insurers.	£25,000

2.14 For the most part, the firms that are dual-regulated with the PRA pay the complex fees, so the other categories largely relate to firms regulated by the FCA alone.

Costs and cost recovery

2.15 The gateway functions are undertaken by our Authorisations Division. The total cost of the Division, including direct charges for staff and indirect charges for IT systems, rent, training and recruitment, was approximately £31m in 2013/14.

2.16 The direct staff costs of the teams undertaking chargeable activities (applications and VoPs) were about £4.5m in 2013/14. Adding in their share of indirect charges brings the total to approximately £7.9m – around a quarter of the total cost of the Authorisations Division.

2.17 Once a firm has been authorised, it is liable to pay us annual periodic fees. Those authorisation costs that are not recovered directly from applicants are recovered from the wider population of fee-payers through periodic fees. The total revenue from authorisation and VoP application fees was approximately £2.7m in 2013/14, so some 65% of the cost of the teams dealing with these chargeable processes was in practice recovered through periodic fees.

2.18 In the next two chapters, we discuss:

- Distributing the recovery of authorisation costs between different fee-payers.
- Suggestions for revising application fees.

3. Distributing the recovery of authorisation costs between different fee-payers

3.1 Applicants for authorisations and VoPs paid only 35% of the overall processing costs in 2013/14, as explained in paragraph 2.17. The balance was paid by existing firms through periodic fees. Higher periodic fees might constitute a regulatory barrier if they were sufficiently material to affect firms' decisions to enter into and expand within a market. Also, we put forward the hypothesis in paragraph 2.4 that the absolute level of application fees might represent a material consideration for smaller firms but less so for larger ones. This chapter discusses different ways we might distribute the recovery of the costs of authorisation between fee-payers.

Policy background

3.2 Our application fee rates and the underlying policies are largely unchanged since the first FSA consultation paper on fees in 2000 (CP56). In this, the FSA set out the principle that the costs of applications should be shared between new applicants and existing fee-payers. It considered three options:

- Full recovery of costs from applicants.
- No recovery of costs from applicants, with all costs borne by existing firms.
- Partial recovery of costs from applicants, with the balance paid by existing firms.

3.3 CP56 recommended the third option. It acknowledged that full recovery of costs from applicants would ensure users paid for the processes they had requested and it would discourage what the CP described as 'frivolous applications'. However, it stressed that the authorisation process was intended to support the market as a whole, with firms that are already authorised benefiting from our scrutiny of applicants seeking to enter their markets. If new entrants meet minimum standards, that reduces the risk of firm failure and keeps down compensation scheme costs; and, it helps to protect consumers and maintain market confidence.

3.4 Significant application costs might discourage market entry, with an adverse effect on competition and innovation. The CP acknowledged that charging no application fees and recovering all the costs from existing fee-payers would avoid this risk, but concluded it was 'less likely to discourage frivolous applications (with a resulting non-productive use of resources).' The CP also considered it might be unfair on existing market participants, most of whom had paid an entrance fee in the past.

3.5 When reviewing the consultation responses in December 2000 (CP79), the FSA reported that opinion was split almost evenly, with 48% of responses favouring full recovery from applicants and 50% favouring shared cost recovery. The larger firms tended to prefer full cost recovery from applicants. There was little support for charging no application fees. After considering the arguments and looking at current regulatory practice, the FSA opted for shared recovery, which remains the practice of both the FCA and PRA.

3.6 CP56 had proposed that the costs should be split equally between new applicants and existing fee-payers. CP79 reported that responses from firms indicated a view that the more complex firms should bear a larger part of the costs. So, the FSA proposed a gradation in the split, with complex applications bearing 90% of the application cost, moderately complex 70% and straightforward 50%.

3.7 Following a review of application fees in 2006-07, the FSA decided to abandon the attempt to link the charges to actual costs because, if fees moved up or down each year as processing resources changed, that would not give firms the year-on-year stability they needed when considering entry to the market. Rather than a fixed relationship between costs and the applicant's share of the fee, CP07/03 (*Regulatory fees and levies 2007/08*, February 2007) proposed instead a 'fair apportionment' between application fees and periodic fees.

Sharing costs between applicants and existing fee-payers

3.8 If the cost to the direct entrant is reduced, the balance is transferred to the annual periodic fees, though the cost is then distributed across a much larger population of firms.

3.9 In practice, our modelling indicates that the impact on periodic fees is marginal. Approximately 40% of firms pay only the minimum periodic fee of £1,000, so they are not affected. However, even if we were to charge no application fees at all, the effect would be to raise the periodic fees paid by firms above minimum fee thresholds by only 0.4%.

3.10 If we were instead to recover all the processing costs from applicants, the benefit for existing firms would be almost equally small. It would reduce periodic fees by just 0.8%. Such small changes in ongoing regulatory compliance costs are unlikely to have an effect on a firm's decision to enter or expand in a market.

3.11 We have already discussed our hypothesis that application fees are more likely to be a significant factor in the decision-making of smaller firms. If that is correct, the distribution of fees between smaller and larger applicants would be more significant than the distribution between new applicants and existing firms.

Sharing costs between more and less complex applications

3.12 To stimulate discussion about the different ways we could balance cost recovery between applicants, we have set out seven scenarios in Table 3.1. We have based them on the complexity categories as they now stand and the 2013/14 case load. We have defined full cost recovery as the £7.9m cost (including overheads) of employing the teams that processed authorisations and VoPs in 2013/14.

3.13 The main features of Table 3.1 are:

- *Scenarios 1 to 3*: make no change in the current relationships between the complexity categories. Scenario 1 shows what we would charge if we increased each category sufficiently to achieve full cost recovery. Scenario 2 increases the current rates in line with inflation and Scenario 3 doubles them.

- *Scenario 4*: shows no charge to applicants. Free applications would avoid any risk that fees might discourage market entry and innovation. On the other hand, it could be argued that an application fee that is significant enough creates an incentive for a firm to ensure that its application is good quality, as it will incur a cost if it is not. It also creates a disincentive for a firm to apply for an application prematurely (e.g. before its business model has been properly developed), because the application is likely to be refused and the fee will not be refunded.

- *Scenarios 5 to 7*: show how we might have achieved full cost recovery while restructuring the charges towards the more complex categories of application. In Scenario 5, we reduce the straightforward fee to align it with the lowest of the straightforward application fees we introduced for consumer credit firms from April this year, while Scenario 6 reduces it to the middle of the range of consumer credit application fees. Consumer credit application fees are based on income and the straightforward category ranges from £600 for firms with under £50,000 of consumer credit business to £5,000 for firms with over £1 million. Scenario 7 holds straightforward fees at their current level.

3.14 The scenarios are based on the application fees as they now stand. In the next chapter, we consider some options for revising our charging policy.

3.15 We would appreciate comments on the different approaches illustrated through the scenarios and any other aspects of this chapter. In particular, we pose the following questions:

Q1: **What are your views on the principle that the costs of processing applications should be shared between applicants and existing firms, rather than recovering all the costs from applicants?**

Q2: **Do you have any views on the advantages and disadvantages of charging no application fees? For example, might it encourage innovation and wider participation in markets? Alternatively, might it encourage unrealistic applications from firms with little prospect in practice of meeting our threshold conditions?**

Q3: **Are you able to offer us any evidence about the significance of our application fees in comparison with the overall cost of setting up a new business and the other costs involved in preparing a firm for authorisation?**

Q4: **Are you able to give us any insights into the significance of our application fees in relation to the wider costs of meeting our threshold conditions and complying with our ongoing regulatory and reporting requirements?**

Q5: **Do you have any views on whether we should weight cost recovery more heavily towards the more complex applications, holding down or even reducing the fees for straightforward applications?**

Q6: **Do you have any other comments arising out of the illustrations presented through the scenarios in Table 3.1?**

Table 3.1: Scenarios to illustrate impact of different assumptions on current application fees, using 2013/14 data

Fee	Current rate	Modelled rate based on scenario (rounded)	Increase	Costs recovered from applicants	Revenue recovered from application charges
1. Full cost recovery from applicant, applied equally to all fees					
Straightforward	£1,500	£4,300	187%	100%	£7.9 m
Moderately complex	£5,000	£14,350	187%		
Complex	£25,000	£71,750	187%		
2. Inflation adjusted					
Straightforward	£1,500	£2,000	36%	50%	£4.0 m
Moderately complex	£5,000	£6,800	36%		
Complex	£25,000	£33,900	36%		
3. Double fees					
Straightforward	£1,500	£3,000	100%	70%	£5.5 m
Moderately complex	£5,000	£10,000	100%		
Complex	£25,000	£50,000	100%		
4. No application fees					
Straightforward	£1,500	£0	-100%	0%	£0
Moderately complex	£5,000	£0	-100%		
Complex	£25,000	£0	-100%		

5. Aligned with lowest consumer credit straightforward fee, full cost recovery					
Straightforward	£1,500	£600	-60%	100%	£7.9 m
Moderately complex	£5,000	£29,350	487%		
Complex	£25,000	£146,750	487%		
6. Aligned with medium consumer credit straightforward fee, full cost recovery					
Straightforward	£1,500	£1,000	-33%	100%	£7.9 m
Moderately complex	£5,000	£27,850	457%		
Complex	£25,000	£139,250	457%		
7. Hold straightforward fee at current level, full cost recovery					
Straightforward	£1,500	£1,500	0%	100%	£7.9 m
Moderately complex	£5,000	£25,970	419%		
Complex	£25,000	£130,00	419%		

4.
Suggestions for revising application fees

4.1 As explained in paragraph 1.10, our application fees have been eroded by about a third through inflation. Paragraph 2.17 confirmed that they do not reflect our actual processing costs. In this chapter, we set out some suggestions we have considered for revising our application fees. We would welcome comments on these and ideas for additional options.

4.2 Some firms have told us that they would be prepared to pay extra to have their applications fast-tracked. We have discussed this in depth internally and have decided it is not an option we should pursue because it is not realistic or fair:

- Our priority should be to improve our services for all firms. If we put greater resources into processing one group of applicants then, regardless of how it was being paid for, we would be taking resources away from other applicants; and, if we prioritise one group then, other things being equal, we must by definition be deprioritising another.
- Consequently, this would conflict with our competition objective. We would not be maintaining a level playing field if we gave an advantage to firms that were able to pay extra.
- It is not a commitment we could meet in practice. We do not know until an application is submitted how closely it matches our threshold conditions. We could not honour a commitment to complete an application more quickly while we still had unresolved questions about the firm's suitability.

Weight fees towards more complex applications

4.3 Improvements to our systems, including the implementation of a new case management system and tighter definitions of the most critical risks to our objectives, will enable us to streamline the process for assessing our most straightforward applications, especially applications from appointed representatives (ARs) who are seeking full authorisation. To reflect this in our fee structure, we could introduce a new category below the straightforward fee.

4.4 Table 4.1 sets out four scenarios to illustrate how we might incorporate a 'very straightforward' fee into the existing categories, using 2013/14 data. All of the scenarios suggest at the same time weighting cost recovery towards the more complex applications.

4.5 Scenario A sets the very straightforward category on a level with the lowest consumer credit application fee and reduces the straightforward category to the mid-level consumer credit straightforward fee. Scenarios B to D hold the very straightforward fee to the current straightforward level and look at different ways of adjusting the higher categories.

Table 4.1: Scenarios to illustrate the introduction of a 'very straightforward' fee, using 2013/14 data

Fee	Current rate	Modelled rate based on scenario	Increase	Costs recovered from applicants	Revenue recovered from application charges
A. Align with lowest consumer credit fees					
Very straightforward	---	£600	N/A	61%	£4.8m
Straightforward	£1,500	£1,000	-33%		
Moderately complex	£5,000	£15,000	200%		
Complex	£25,000	£100,000	300%		
B. Align with current straightforward fee					
Very straightforward	---	£1,500	N/A	89%	£7.0m
Straightforward	£1,500	£2,250	50%		
Moderately complex	£5,000	£20,000	300%		
Complex	£25,000	£100,000	300%		
C. Staged increase					
Very straightforward	---	£1,500	N/A	83%	£6.5m
Straightforward	£1,500	£3,000	100%		
Moderately complex	£5,000	£15,000	200%		
Complex	£25,000	£100,000	300%		
D. Staged increase, moderated complex fee					
Very straightforward	---	£1,500	N/A	66%	£5.3m
Straightforward	£1,500	£2,250	50%		
Moderately complex	£5,000	£12,500	150%		
Complex	£25,000	£75,000	200%		

Scale of business

4.6 The application fees we introduced for firms seeking consumer credit permissions from 1 April 2014 take account of their scale of business, using income as a measure. For example, firms that make straightforward applications pay only £600 if their projected consumer credit income is £50,000 or less, but £5,000 if their income is over £1 million. The highest consumer credit application fee is £15,000, for complex applications by firms with over £1 million of income, compared with £25,000 for non-consumer credit complex applications.

4.7 On the basis of our experience, we believe it is not necessary to scale non-consumer credit fees according to the size of projected business. The great majority of sole traders in the 'A' fee-blocks are intermediaries, falling into the straightforward category. A self-employed deposit-

taker in the complex category would not be plausible. By contrast, a large number of high-cost, short-term lenders in the consumer credit 'complex' category are self-employed or very small firms, which is why we decided it was necessary to introduce a distinction based on income for consumer credit applications.

Charging for scaling down

4.8 We do not charge firms that are reducing their permissions or seeking to exit the market altogether. We appreciate that moving out of a particular sector of a market often reflects a straightforward business decision to change a firm's focus and should not be assumed to indicate financial difficulty, but we follow the general principle that we should avoid adding to the costs of a firm that is scaling down its activities. In some cases, firms will indeed be in difficulties and may not have cash if they are in the process of winding up.

Costs of dealing with changes in control

4.9 Firms are required under the Acquisitions Directive to notify us of any potential change in their control – for example, through a merger or acquisition. There is no standard charge for dealing with this, but in the case of a large or complex business, we may have to invest a large amount of time and resources into understanding the full implications of the changes, re-assessing the firm's continued ability to meet our threshold conditions and keeping in touch with circumstances that may be rapidly evolving. As well as our own staff costs, we may have to engage independent professional advisors such as lawyers and accountants.

4.10 If our costs go above £50,000, we are able to initiate a special project fee (SPF) to recover them from the firm itself. Otherwise, the costs fall to the wider body of fee-payers. In practice, an SPF has only been applied on one occasion to recover the costs of a change in control.

4.11 A standard fee for processing changes in control would reduce the charges to other firms but introducing a fee presents practical challenges. For example, we would be charging firms for an action they are legally obliged to perform, while there is a risk that a fee might discourage them from doing so, even though that would be a criminal offence. In addition, we may not be aware of the complexity of a case until after we start working with the firm. Having charged the standard fee, it might turn out that this was insufficient. If an authorised firm was the target of a hostile take-over by a firm that was not authorised, we would be unable to enforce payment of any fee by the non-authorised initiator. It might seem unreasonable to charge a target firm that was resisting the change, and might even be construed as an intervention against it.

4.12 We would welcome any views on the appropriateness and practicality of charging fees for changes in control.

Stability of application fees

4.13 Our moderately complex and complex fees have remained unchanged since 2001 and our straightforward fees since 2004. In practice, then, there has been stability in our pricing, but we did not make a commitment to maintain that stability. One option might be to set the fees for a period – say, three years – and then review them. Another might be to raise them in line

with inflation – again, with periodic reviews. In either case, we would need to reserve the right to amend the policy if circumstances change. We would welcome views on whether firms would value a commitment along these lines.

Questions for discussion

4.14 Our questions for discussion are:

Q7: Do you have any comments on the issues we present in chapter 4 and/or any other suggestions for recovering the costs of authorisation?

Q8: Do you have any comments arising out of the illustrations presented through the scenarios in Table 4.1?

Q9: Do you have any views on the appropriateness and practicality of charging for changes in control?

5.
Next steps

5.1 We are presenting these issues to stimulate debate and we welcome comments and further suggestions. We will take the responses into account when preparing proposals for consultation in October 2014.

5.2 We are conscious that most readers of our discussion papers are likely to be firms that are already authorised by us. We are particularly keen to hear from businesses that are considering applying to us, or have in the past decided against applying to us, so that we can get insights into the role the application fees play, if any, in firms' decision-making processes.

5.3 Please send your response to us by **22 August 2014**. Please note that we will share the responses with the PRA, unless you make it clear that you do not wish us to do so.

Annex 1
List of questions

Q1: What are your views on the principle that the costs of processing applications should be shared between applicants and existing firms, rather than recovering all the costs from applicants?

Q2: Do you have any views on the advantages and disadvantages of charging no application fees? For example, might it encourage innovation and wider participation in markets? Alternatively, might it encourage unrealistic applications from firms with little prospect in practice of meeting our threshold conditions?

Q3: Are you able to offer us any evidence about the significance of our application fees in comparison with the overall cost of setting up a new business and the other costs involved in preparing a firm for authorisation?

Q4: Are you able to give us any insights into the significance of our application fees in relation to the wider costs of meeting our threshold conditions and complying with our ongoing regulatory and reporting requirements?

Q5: Do you have any views on whether we should weight cost recovery more heavily towards the more complex applications, holding down or even reducing the fees for straightforward applications?

Q6: Do you have any other comments arising out of the illustrations presented through the scenarios in Table 3.1?

Q7: Do you have any comments on the issues we present in chapter 4 and/or any other suggestions for recovering the costs of authorisation?

Q8: Do you have any comments arising out of the illustrations presented through the scenarios in Table 4.1?

Q9: Do you have any views on the appropriateness and practicality of charging for changes in control?

Annex 2
Compatibility with the general duties of the FCA

1. This Annex explains our reasons for concluding that the topics we are putting forward for discussion are compatible with certain requirements under the Financial Services and Markets Act 2000 (FSMA), as amended by the 2012 Act, and with the duty on the FCA to discharge its general functions in a way which promotes effective competition in the interests of consumers (s.1B(4)). This duty applies in so far as promoting competition is compatible with advancing the FCA's consumer protection and/or integrity objectives.

2. This annex further includes our assessment of the equality and diversity implications of this discussion paper.

The FCA's objectives and regulatory principles

3. Our authorisations policies and procedures form the gateway through which we control the entry of all firms to the market, and so they are integral to all of our operational objectives:

   - Delivering consumer protection – securing an appropriate degree of protection for consumers.
   - Enhancing market integrity – protecting and enhancing the integrity of the UK financial system.
   - Building competitive markets – promoting effective competition in the interests of consumers.

4. We believe this paper is most relevant to the third objective since we are seeking views on how we should recover the costs of the gateway. Application fees, for example, might influence firms' decisions to enter particular markets. If our charges deterred firms from entering particular markets, this could restrict competition, with implications for consumer outcomes. We have presented a number of different charging structures to stimulate discussion on how our authorisation charges might be re-structured to avoid any risk that they might constitute a potential barrier to market entry.

5. In preparing this paper, we have had regard to the regulatory principles set out in s.3B FSMA. The most relevant are considered below:

   - *The need to use our resources in the most efficient and economical way* – we continuously work to improve the efficiency and effectiveness of our operations and systems. In chapter 4 we suggest that we might be able to take advantage of the improvements we have made by introducing a lower fee category for smaller firms.

- *The principle that a burden or restriction should be proportionate to the benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction* – our focus in this paper is to invite views on how we should ensure that the costs of the gateway are borne by those best able to meet them, whether by sharing costs with the larger body of existing fee-payers, or recovering a greater proportion of the costs from larger applicants, or both.

- *The desirability of exercising our functions that recognises differences in the nature of the businesses carried on by different persons we regulate* – our complexity categories are intended to reflect the differences in the nature of the different businesses.

- *The principle that we should exercise our functions as transparently as possible* – this discussion paper is in itself intended as an exercise in transparency.

Expected effect on mutual societies

6. The discussion in this paper does not directly affect mutual societies, although any insights emerging from the discussion process might be applied to them in the future.

Compatibility with the duty to promote effective competition in the interests of consumers

7. As explained in paragraph 4 above, the issues raised in this paper directly address the promotion of competition in the interests of consumers since application fees could influence firms' decisions to enter markets. We are seeking views on whether this is in practice the case, and whether we should restructure the fees to reduce such risks.

Equality and diversity

8. We are required under the Equality Act 2010 to have due regard to the need to eliminate discrimination and to promote equality of opportunity in carrying out our policies, services and functions. We would welcome comments on the conclusion of our equality impact assessment that 'straightforward' application fees are likely to be relevant to the equalities agenda because they are most commonly paid by sole traders and small firms, among whom we believe groups with protected characteristics may be disproportionately represented. We will carry out a new equality impact assessment in the light of the comments received when we formulate our proposals for consultation in October.

Financial Conduct Authority

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25 The North Colonnade Canary Wharf
London E14 5HS
Telephone: +44 (0)20 7066 1000
Website: www.fca.org.uk
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