Payments and Digital Assets Authorisations Video Transcript - Threshold conditions with Val Smith, Head of Authorisations: Part 1

Louis Myers

- If you're watching this, you're likely at the start of your authorisation journey and understanding the threshold conditions is one of the most important first steps you can take. These conditions exist to ensure that firms entering the market are properly equipped to protect their customers and to maintain the integrity of UK financial markets. And that's why getting this right matters so much. Firms that don't meet these standards will not be authorised. My name's Louis. Today I'm joined by Val Smith who will help us understand what the threshold conditions are, and most importantly, how we assess them in practise.

Val Smith

- Thank you very much, Louis. It's a pleasure to speak with you today. And I look forward to talking through what we're expecting from people in their application and how they can help ensure that they're getting the right stuff to us.

Louis Myers

- The threshold conditions apply to every single firm, don't they? Regardless of size, it doesn't matter what their business model looks like. That universality is what makes them so important. They're foundational. So let's talk a little bit, Val about what it actually means and what they actually are.

Val Smith

- Certainly, and you're quite right, the TCs, or threshold conditions as we call them, frame our high-level expectations of the firms in our industry.

And just to recap, there are five threshold conditions for firms that are just regulated by the FCA, and they are the business model threshold condition. Is your business sustainable and viable? Appropriate resources, do you have what you need to do the business? Suitability, is what you need suitable to do that business? Location of offices, are they in the right place? And effective supervision. So how we can effectively supervise those firms. And the threshold conditions serve as a common benchmark for us to ensure good consumer and market outcomes. I look at the threshold conditions in conjunction with the permissions or regulated activities that your business will need to do when you're in the financial services perimeter. And those permissions will drive the rules and specific guidance that you'll need to show us when you make your application for authorisation that you can meet. So think about your business in the context of both the threshold conditions and then those rules and guidance that will be driven by what it is you need to do. This will look different in different markets and sectors, but it comes back to where we will start on the business model threshold condition.

Louis Myers

- Thanks, Val. As you've mentioned, there are five threshold conditions. In this particular video, we're going to look at the first two, and then we'll come back in the second part of the video to delve into the remaining three. So as you've said, let's start with the business model. For firms who are new to regulation, this is probably something that they're not really certain about what it means. So what are we actually asking them to do here?

Val Smith

- So when you tell us about how you'll meet this threshold condition, I'd like to know how your strategy is suitable for the regulated activities and permissions that you want to do. And I'm going to be thinking about how that business you want to do, how it fits with the regulatory outcomes and how we ensure that the outcomes for consumers and markets are the ones that we're looking for. So when we look at your strategy in the round, we're going to be thinking, "Is it sustainable and viable and will it deliver good regulatory outcomes?"

Louis Myers

- It might be tempting perhaps to focus on setting out intentions clearly, but I understand there's evidence needed. There's a lot of things that people need to provide. And it might mean that sometimes applications

can run into a bit of difficulty. So in practical terms, what does the assessment look like?

Val Smith

- So things that we will be looking at, we'll start with your regulatory business plan and that's quite critical as it should explain your purpose, what you intend to do and with whom in the market, and how any risks of harm that might come about from that business will be managed by you. So given the business that you want to do, I'm going to be interested in who are the people that are going to do that business and how you have set yourself up with your controls or your systems to manage those risks and provide that service to your customers. I see this regulatory business part as a core part of the narrative for what you want to do and your opportunity to explain how everything comes together and how you will do your business in a way that meets the threshold conditions and our standards.

Louis Myers

- It's really useful, I think, to understand where things can go wrong so firms can learn from others' experience. There must be some common themes, I suppose, when you receive some of these applications. What generally are you looking out for? Are there things that people should be wary of?

Val Smith

- A great application will tell the story in a coherent manner. And in my experience, if you treat your authorisation as a series of separate things that you tick off along the way, rather than building them all together, it is much less effective. And sometimes we see things that are too vague, so not enough detail about how you will be doing things. You might be doing the same product, but with a different customer group and you need to decide what will be different and how you will manage that and explain that to us. Sometimes as well, we see information that could be about your group if you sit alongside other companies, and really we want to understand how you will do things. And if I think particularly in the context of the business model threshold condition, what we're looking for is a strategy that is sustainable and viable. And an example where that might not work is if you come to me and you say, "Do you know what? My business will be viable and sustainable, but only if I sell these particular types of product that could be quite high risk and inappropriate for my customers or consumers." Then I might not think that that is sustainable.

So you need to put all of those things together when you think about this condition.

Louis Myers

- So we've talked a little bit, I suppose, about where people might find difficulty in making a good application. The appropriate resources condition is also an interesting one because I would imagine that people hearing that term for the first time might be thinking, "Ah, I'm talking about capital. I'm talking about money here." But actually, it's not just that, is it? What else are you looking for in this particular condition?

Val Smith

- That's right. It is much broader than capital, although that is really important, but it includes non-financial resources. So your people, your systems, the way you have set yourself up to do your business. But if I start with financial resources, we expect everyone to hold capital just in case something goes wrong. But we will want to look at your financial information to understand how you see your financials play out alongside your business. So when I look at your strategy, it will need to, again, be coherent with the financial information and match up in terms of whether that be growth, product sales, customer size. One of the things that people think is that if they are a new business, they need to be profitable from the beginning. And we accept that that's not always realistic for some businesses. There will be a growth period, but we do need to understand where that point of profitability will come in and that it then matches the story you've told us in your business plan.

Louis Myers

- So we've touched on the financial resources there. They're the more intuitive part, I suppose, of this condition, but there's a very important non-financial side, isn't there? It's probably the less understood element of this particular condition. So what particularly are we looking for?

Val Smith

- So when I think about your non-financial resources, I'm really thinking about how you have set yourself up to deliver and to deliver to meet the regulatory requirements. So who are your people? Do they have the right skills and experience to do the business you have set out for us in your business plan? Are those people designing the right systems and controls that can manage and mitigate the risks that might come from the business that you intend to do? Have you created your governance in the

right way so it's really clear who's making the decisions and how things will happen in your business? And I would ask you as you work through that to think about when you apply for authorisation, are you ready, willing, and organised to be able to be authorised?

Louis Myers

- Thank you, Val, so much for being part of this video. And firms need to be able to understand and provide clear and comprehensive regulatory business plans that tell the full story of their business both now and into the future. And crucially, the financial and non-financial resources they evidence need to match that story convincingly. In our second video, we'll move on to the remaining three conditions: suitability, location of offices, and effective supervision. These can feel more abstract than the conditions that we've covered today, but they are just as important and we'll explore exactly what meeting them looks like in practise.