

Chapter 2

The threshold conditions

2.3 Effective supervision

2.3.1 UK [deleted]

Paragraph 2C of Schedule 6 to the Act

- 2.3.1A UK
- (1) A must be capable of being effectively supervised by the FCA having regard to all the circumstances including-
- (a) the nature (including the complexity) of the regulated activities that A carries on or seeks to carry on;
 - (b) the complexity of any products that A provides or will provide in carrying on those activities;
 - (c) the way in which A's business is organised;
 - (d) if A is a member of a group, whether membership of the group is likely to prevent the FCA's effective supervision of A;
 - (e) whether A is subject to consolidated supervision required under any of the relevant directives;
 - (f) if A has close links with another person ("CL")-
 - (i) the nature of the relationship between A and CL;
 - (ii) whether those links are or that relationship is likely to prevent the FCA's effective supervision of A; and
 - (iii) if CL is subject to the laws, regulations or administrative provisions of a territory which is not an EEA State ("the foreign provisions"), whether those foreign provisions, or any deficiency in their enforcement, would prevent the FCA's effective supervision of A.
- (1A) Paragraphs (a), (b) and (e) of sub-paragraph (1) do not apply where the only regulated activities that the person concerned carries on, or seeks to carry on, are-
- (a) relevant credit activities, and
 - (b) if any, activities to which, by virtue of section 39(1D), sections 20(1) and (1A) and 23(1A) do not apply when carried on by the person.
- (2) A has close links with CL if-
- (a) CL is a parent undertaking of A;
 - (b) CL is a subsidiary undertaking of A;
 - (c) CL is a parent undertaking of a subsidiary undertaking of A;

- (d) CL is a subsidiary undertaking of a parent undertaking of A;
- (e) CL owns or controls 20% or more of the voting rights or capital of A; or
- (f) A owns or controls 20% or more of the voting rights or capital of CL.

2.3.1B G Paragraph 2C of Schedule 6 to the *Act* sets out the effective supervision *threshold condition* for *firms* carrying on, or seeking to carry on, *regulated activities* which do not include a *PRA-regulated activity*.

2.3.1BA G For the purposes of paragraph 2C (1A) of Schedule 6 to the *Act*, relevant credit activity is defined in paragraph 2G of Schedule 6 to the *Act*. Guidance on the meaning of relevant credit activity is given in ■ **COND 1.1A.5A G**.

Paragraph 3B of Schedule 6 to the Act

- 2.3.1C** UK
- (1) B must be capable of being effectively supervised by the FCA having regard to all the circumstances including-
 - (a) the nature (including the complexity) of the regulated activities that B carries on or seeks to carry on;
 - (b) the complexity of any products that B provides or will provide in carrying on those activities;
 - (c) the way in which B’s business is organised;
 - (d) if B is a member of a group, whether membership of the group is likely to prevent the FCA’s effective supervision of B;
 - (e) whether B is subject to consolidated supervision required under any of the relevant directives;
 - (f) if B has close links with another person (“CL”)-
 - (i) the nature of the relationship between B and CL;
 - (ii) whether those links are or that relationship is likely to prevent the FCA’s effective supervision of B; and
 - (iii) if CL is subject to the laws, regulations or administrative provisions of a territory which is not an EEA State (“the foreign provisions”), whether those foreign provisions, or any deficiency in their enforcement, would prevent the FCA’s effective supervision of B.
 - (2) B has close links with CL if-
 - (a) CL is a parent undertaking of B;
 - (b) CL is a subsidiary undertaking of B;
 - (c) CL is a parent undertaking of a subsidiary undertaking of B;
 - (d) CL is a subsidiary undertaking of a parent undertaking of B;
 - (e) CL owns or controls 20% or more of the voting rights or capital of B; or
 - (f) B owns or controls 20% or more of the voting rights or capital of CL.

- 2.3.1D** **G** Paragraph 3B of Schedule 6 to the *Act* sets out the effective supervision *threshold condition* which is relevant to the discharge by the *FCA* of its functions under the *Act* in relation to *firms* carrying on, or seeking to carry on, *regulated activities* which include a *PRA-regulated activity*.
- 2.3.1E** **G** The guidance in **COND 2.3** should be read as applying to both paragraph 2C of Schedule 6 of the *Act* and, as far as relevant to the discharge by the *FCA* of its functions under the *Act* in respect of *firms* carrying on, or seeking to carry on, a *PRA-regulated activity*, paragraph 3B of Schedule 6 of the *Act*.
- 2.3.1F** **G** *Firms* carrying on, or seeking to carry on, a *PRA-regulated activity*, should note that the *PRA* is also responsible for assessing effective supervision under its own *threshold conditions*. Paragraphs 4F and 5F of Schedule 6 to the *Act* set out the effective supervision *threshold conditions* which are relevant to the discharge by the *PRA* of its functions under the *Act* in relation to *firms* carrying on, or seeking to carry on, a *PRA-regulated activity*. For the avoidance of doubt, this *guidance* does not apply to the *threshold conditions* set out in paragraphs 4F and 5F of Schedule 6 to the *Act*.
- 2.3.2** **G** Paragraphs 2C and 3B of Schedule 6 to the *Act* implements requirements of the *Single Market Directives*, but the *Act* extends this condition to *firms* from outside the *EEA* and other *firms* which are outside the scope of the *Single Market Directives*.
- 2.3.3** **G** In assessing the *threshold conditions* set out in paragraphs 2C and 3B of Schedule 6 to the *Act*, factors which the *FCA* will take into consideration include, among other things, whether:
- (1) it is likely that the *FCA* will receive adequate information from the *firm*, and those *persons* with whom the *firm* has *close links*, to enable it to determine whether the *firm* is complying with the requirements and standards under the *regulatory system* for which the *FCA* is responsible and to identify and assess the impact on its *statutory objectives*; this will include consideration of whether the *firm* is ready, willing and organised to comply with *Principle 11* (Relations with regulators and the *rules* in *SUP* on the provision of information to the *FCA*;
 - (2) the structure and geographical spread of the *firm*, the *group* to which it belongs and other *persons* with whom the *firm* has *close links*, might hinder the provision of adequate and reliable flows of information to the *FCA*; factors which may hinder these flows include the fact there may be branches or connected *companies* in territories which supervise *companies* to a different standard or territories with laws which restrict the free flow of information, although the *FCA* will consider the totality of information available from all sources; and
 - (3) [deleted]
 - (4) in respect of a *firm* not carrying on, or seeking to carry on, a *PRA-regulated activity*, it is possible to assess with confidence the overall financial position of the *group* at any particular time; factors which may make this difficult include lack of audited consolidated accounts

for a *group*, if companies in the same *group* as the *firm* have different financial years and accounting dates and if they do not share common auditors.

2.3.4 **G** [deleted]

2.3.5 **G** [deleted]

Meaning of "parent undertaking" and "subsidiary undertaking"

2.3.6 **G** (1) Section 420(1) of the *Act* (Parent and subsidiary undertaking) states that, except in relation to an *incorporated friendly society*, 'parent undertaking' and 'subsidiary undertaking' have the same meaning as in the Companies Acts (see section 1162 of, and schedule 7 to, the Companies Act 2006). These are the cases referred to in ■ COND 2.3.7 G (1)(a) to ■ (f).

(2) Section 420(2) of the *Act* supplements these definitions in two ways; these are the cases referred to in ■ COND 2.3.7 G (1)(g) and ■ (h).

(3) Paragraph 1A of Schedule 6 to the *Act* extends the meaning of 'subsidiary undertaking' for the purposes of the *threshold conditions* to all the cases in articles 1(1) and (2) of the *Seventh Company Law Directive* in which one *undertaking* may be a *subsidiary* of another *undertaking* (see ■ COND 2.3.11 G).

2.3.7 **G** (1) For the purposes of the *threshold conditions* set out in paragraphs 2C and 3B of Schedule 6 to the *Act*, and except in relation to an *incorporated friendly society*, an *undertaking* is a *parent undertaking* of another *undertaking* (a *subsidiary undertaking*) if any of the following apply to it:

- (a) it holds a majority of the voting rights in the *subsidiary undertaking*; or
- (b) it is a member of the *subsidiary undertaking* and has the right to appoint or remove a majority of its board of *directors*; or
- (c) it has the right to exercise a dominant influence over the *subsidiary undertaking* through:
 - (i) provisions contained in the *subsidiary undertaking's* memorandum or articles; or
 - (ii) a control contract; or
- (d) it is a member of the *subsidiary undertaking* and controls alone, under an agreement with other shareholders or members, a majority of the voting rights in the *subsidiary undertaking*; or
- (e) it has the power to exercise, or actually exercises, dominant influence or control over it, or it and the *subsidiary undertaking* are managed on a unified basis; or
- (f) it is a *parent undertaking* of a *parent undertaking* of the *subsidiary undertaking*; or
- (g) it is an individual and would be a *parent undertaking* if it were an *undertaking*; or

- (h) it is incorporated in or formed under the law of another *EEA State* and is a *parent undertaking* within the meaning of any rule of law in that State for purposes connected with implementation of the *Seventh Company Law Directive*.
- (2) [deleted]
- 2.3.8** G (1) In relation to ■ COND 2.3.7 G (1)(b) and ■ (d), an *undertaking* is treated as a member of another *undertaking* if any of its *subsidiary undertakings* is a member of that *undertaking*, or if any shares in that other *undertaking* are held by a *person* acting on behalf of the *undertaking* or any of its *subsidiary undertakings*.
- (2) [deleted]
- (3) [deleted]
- 2.3.9** G The provisions of Schedule 7 to the Companies Act 2006 (Parent and subsidiary undertakings: supplementary provisions) explain and supplement the provisions of section 1162 of the Companies Act 2006 (outlined in ■ COND 2.3.7 G (1)(a) to ■ (f)).
- 2.3.10** G Section 420(3) of the Act (Parent and subsidiary undertaking) states that an *incorporated friendly society* is a *parent undertaking* of another *body corporate* (a *subsidiary undertaking*) if it has the following relationship to it:
- (1) it holds a majority of the voting rights in the *subsidiary undertaking*;
or
- (2) it is a member of the *subsidiary undertaking* and has the right to appoint or remove a majority of the *subsidiary undertaking's* board of *directors*; or
- (3) it is a member of the *subsidiary undertaking* and controls alone, under an agreement with other shareholders or members, a majority of the voting rights in it.
- 2.3.11** G For the purposes of the *threshold conditions* set out in paragraphs 2C and 3B of Schedule 6 to the Act, an *undertaking* is a *subsidiary undertaking* of another *undertaking* if:
- (1) the other undertaking (its parent) is a member of the *undertaking*;
- (2) a majority of the *undertaking's* board of *directors* who have held office during the financial year and during the preceding financial year have been appointed solely as a result of the exercise of the parent's voting rights; and
- (3) no one else is the *parent undertaking* of the *undertaking* under ■ COND 2.3.7 G (1)(a) or ■ COND 2.3.10 G (1).
- 2.3.11A** G Paragraphs 2C(2)(e) and (f) and 3B(2)(e) and (f) of Schedule 6 to the Act reflect legislation initially introduced in the *Post-BCCI Directive*, which

defines close links, in part, by reference to participation. Recital 5 of the *Post-BCCI Directive* gives further guidance on what is meant by 'participation' for the purposes of the directive. It states that the sole fact of having acquired a significant proportion of a company's capital does not constitute participation for the purposes of the directive if that holding has been acquired solely as a temporary investment which does not make it possible to exercise influence over the structure or financial policy of the undertaking.

2.3.12

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The *guidance* in ■ COND 2.3 is not comprehensive and is not a substitute for consulting the relevant legislation, for example the Companies Act 2006, the Friendly Societies Act 1992 and the *Seventh Company Law Directive*, or obtaining appropriate professional advice.