Defining materiality in safeguarding customer funds under CASS 15

A Guidance Note for Members of The Payments Association

Purpose of this guidance

This document provides practical guidance to regulated payment and e-money firms on how to interpret and apply the concept of '*materiality'* in the context of safeguarding customer funds under the Financial Conduct Authority's ("FCA") CASS 15 regime.

Table of Contents

Regulatory context

The FCA has introduced CASS 15 via PS25/12, setting out enhanced safeguarding requirements for payments and e-money firms.

A key feature of the regime is the introduction of notification triggers based on *'material'* failures, including under CASS 15.8.60R.

However:

- There is no prescribed definition of *'material'* breach
- There are no fixed thresholds or quantitative benchmarks
- Firms are expected to apply judgment within an outcomes-based framework

This approach is reinforced by guidance from the Financial Reporting Council ("FRC"), which explicitly requires auditors to exercise professional judgment, rather than rely on rigid criteria.

What the rules require

Under CASS 15.8.60R, firms must notify the FCA without delay where there is a material issue, including where:

- Safeguarding records are *materially* inaccurate, invalid, or out of date
- The firm *materially* fails to perform internal or external reconciliations
- There is a *material* failure to:
    - resolve reconciliation discrepancies
    - top up shortfalls
    - withdraw excess funds
- The firm identifies a *material* difference between safeguarded funds and required amounts over the previous 12 months

Importantly, the rules focus less on numerical thresholds and more on:

- Control effectiveness
- Accuracy of records
- Timeliness of remediation
- Risk to customer funds

A useful way to interpret *'materiality'* under CASS 15 is that it is not purely a measure of size - it is a measure of impact on safeguarding integrity and customer fund protection.

Materiality thresholds vs breaches in the audit report

A common source of misunderstanding is the distinction between breaches that must be notified to the FCA, and breaches that are included in the auditor's report submitted to the FCA.

The auditor's report includes *all* CASS breaches identified during the reporting period, regardless of whether they are considered material. In contrast, material breaches must be notified to the FCA *without delay*, meaning notification is typically made shortly after the regulated firm identifies and classifies the breach as material.

Learnings from CASS 7 (Client money regime)

CASS 15 has a strong parallel with the long-standing client money regime (CASS 7). Historically, the FCA has supervised client assets based on:

1. Adequacy of systems and controls
2. Compliance with rules
3. Transparency of breach reporting

Critically, a*ll breaches* are recorded and reported in audits, regardless of materiality. This same architecture now applies to safeguarding under CASS 15.

A framework for assessing materiality

Firms should adopt a multi-factor assessment framework. Materiality should be determined by considering a combination of dimensions, such as:

1. Financial Impact – What is the absolute size of the shortfall or discrepancy? What is that relative to the scale of safeguarded funds at the firm.

2. Duration - How long has the issue persisted? Was the breach promptly identified and resolved?

3. Customer fund risk - Were customer funds actually at risk? Was there a delay or risk in returning funds?

4. Integrity of books and records - Does the issue undermine confidence in safeguarding records? Could customer entitlements still be accurately determined?

5. Reconciliation effectiveness - Was the firm able to perform the required reconciliations? Were discrepancies identifiable and explainable?

6. Need for firm funding - Was a top-up from own funds required? Does this indicate control weakness?

7. Recurrence and systemic issues - Is the issue isolated or repeated? Does it indicate broader control failure?

8. Insolvency readiness - Would the issue impair: (i) identification of safeguarded funds? (ii) segregation of funds? (iii) timely return to customers in insolvency? This aligns closely with the 'insolvency mindset' expected by auditors.

For further context, a small numerical shortfall may still be material if it reveals systemic reconciliation failures and/or records cannot reliably identify customer balances.

On the flip side, a larger one-off discrepancy may be assessed differently if it is quickly identified, fully understood, promptly remediated, and appears isolated.

Governance expectations

Given the absence of a formal definition, firms are expected to demonstrate discipline and consistency in judgment. At a minimum, firms should implement:

A. A documented materiality framework

One that is approved by senior governance (e.g. Board or Risk Committee), and it clearly sets out the (i) assessment criteria; (ii) escalation thresholds for senior manager escalation, and FCA notification; and (iii) the decision-making process.

B. Incident-level documentation

For each breach or discrepancy:

- What happened
- Root cause
- Impact assessment
- Materiality conclusion
- Rationale for notification (or non-notification)

C. Consistency of Application

- Similar issues should lead to consistent conclusions
- Deviations must be explainable

Safeguarding auditors will review all breaches, not just material ones. They will assess whether the firm's materiality judgments were reasonable, and challenge decisions not to notify the FCA. This reinforces the need for robust documentation, clear reasoning, and evidence-based decisions.

Conclusion and recommended approach

CASS 15 deliberately avoids defining materiality. This reflects the FCA's preference for:

- Outcome-based regulation
- Judgment-led decision-making
- Focus on customer protection

The most effective approach for firms is to:

- Develop a **structured, multi-factor materiality framework** (see above)

- Anchor decisions in:
    a) customer harm
    b) safeguarding integrity
    c) control effectiveness
    d) insolvency readiness

- Ensure decisions are:
    a) well-governed
    b) consistently applied
    c) clearly documented

Firms that can demonstrate clear reasoning, strong controls, and timely escalation are best positioned to withstand both audit scrutiny and FCA supervisory challenge.