Regulatory Policy Committee

Small and Micro Business Assessments: guidance for departments, with case history examples

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Contents

Purpose of this document

This document provides guidance for departments in carrying out a small and micro businesses assessment (SaMBA). In particular, it sets out the steps that departments need to undertake and indicates the type of evidence and analysis that the RPC will be looking for in its scrutiny. The document incorporates the key flowchart and checklist produced in collaboration with BRE and in consultation with departments. The document includes a number of case studies to illustrate aspects of the approach and analysis that departments should undertake. The document will form part of the updated RPC case histories volume but can also be used as a standalone guidance paper.

What are small and micro businesses and why do they matter?

Small businesses are defined in the better regulation framework guidance as those employing between 10 and 49 full-time equivalent (FTE) employees. Micro-businesses are those employing between one and nine employees. Small and micro businesses include voluntary and community bodies (also known as civil society organisations).

The RPC recognises that these definitions might not always work perfectly as an indicator of small and micro businesses (SMBs). In some instances, classification in terms of number of FTE employees might present difficulties and uncertainties, for example, for the gig economy, franchises, companies that employ seasonal workers or businesses that employ few people but have a large turnover or market share. In these situations, departments should explain the definition adopted for SMBs and why it is appropriate. In these situations, the RPC would encourage departments to adopt an inclusive approach to defining and assessing impacts on SMBs.

SMBs make up 99 per cent of UK businesses and account for around 48 per cent employment and 33 per cent of turnover.[1] SMBs often cite regulation as one of the key barriers to growth, and regulation can affect them disproportionately.

[1]House of Commons Library. 12th December 2018. 'Business Statistics', Briefing Paper Number 06152. https://researchbriefings.file.parliament.uk/documents/SN06152/SN06152.pdf

What is a small and micro business assessment and when is it required?

A **small and micro business assessment** (SaMBA) should be used to help understand the impact of a proposal on SMBs and consider whether the proposal will affect SMBs in a different way to medium and large businesses. An objective of a SaMBA is to encourage departments to think specifically about the impacts of a proposal on SMBs. The SaMBA forms part of the impact assessment and has been mandatory for larger domestic regulatory proposals coming into force after March 2014. The better regulation framework guidance states (paragraph 2.3.6): "*A SaMBA is mandatory for all domestic measures that require clearance from the Reducing Regulation Cabinet sub-Committee (RRC) and which have an impact on business greater than the ±£5m EANDCB threshold. Departments should also consider the impact on small and micro-businesses of regulatory policy which is below the threshold, and conduct an assessment where appropriate*."

SaMBA and proportionality

The analysis for a SaMBA should, as with that for the impact assessment as a whole, be proportionate. 'Proportionality' usually refers to the level of evidence and analysis expected according to the scale of the impact of a measure. In general, for a high-impact proposal (for example, with an EANDCB greater than +/- £50 million), the RPC would expect to see a relatively detailed SaMBA. Similarly, for a low-impact measure, a much lower level of evidence and analysis may be sufficient. In either case, it is important for departments to demonstrate that the proposal's impacts on SMBs have been considered in a proportionate way. A higher level of evidence and analysis might be appropriate for low, net-impact measures that are, for example, novel, contentious or have significant distributional impacts. Please see the RPC's proportionality guidance for more information.

Measures that are clearly beneficial to SMBs might not require as much SaMBA analysis, even if they are high impact; for example, it might be relatively straightforward to demonstrate that exemption or mitigation (see below) are not necessary or appropriate. There might also be measures that are aimed at SMBs and/or where all impacts fall on SMBs, where departments might consider that the whole IA relates to SMBs. In these cases, there might be limited need for additional analysis in a SaMBA section. However, in these cases, it should be made clear how the whole IA relates to SMBs and how the underlying requirements of a SaMBA have been met. There might also be value in considering whether there are significant distributional impacts within SMBs.

SaMBA and the RPC

For measures meeting the better regulation framework guidance criterion above, the SaMBA, as part of the IA, is subject to RPC scrutiny at the final stage. The RPC also provides scrutiny of SaMBAs at the consultation stage, where departments have chosen to submit their IA for formal or informal scrutiny.

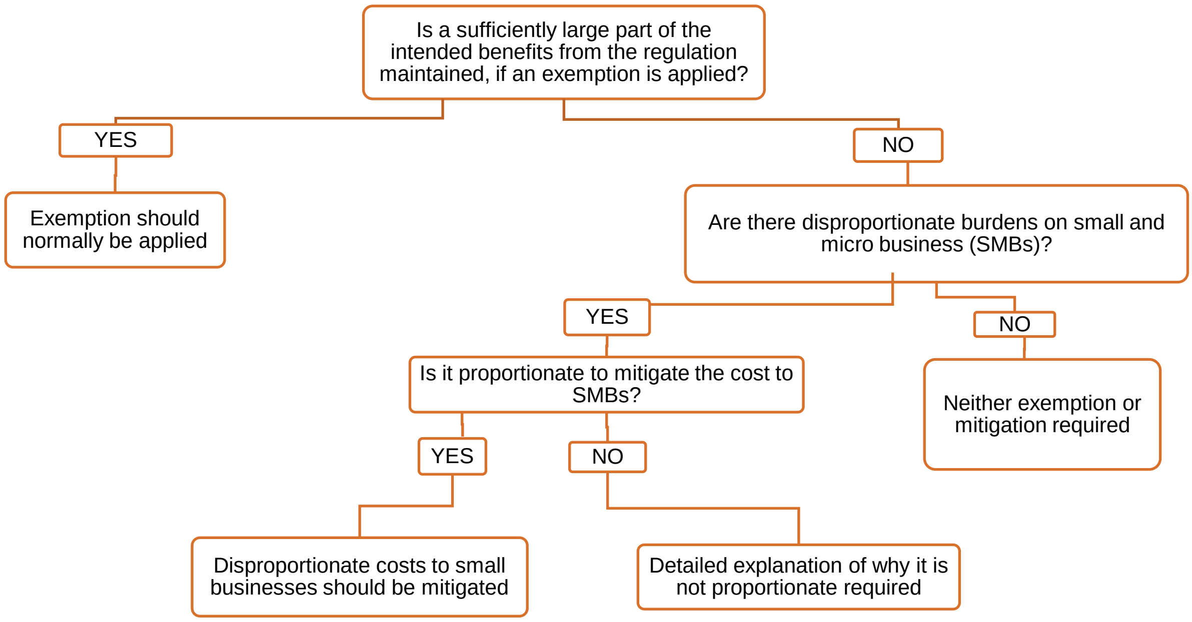
The RPC can red-rate an IA on the quality of its SaMBA if it is considered not fit for purpose. Common red-rated points include not providing any indication of the likely number of small businesses affected or the scale of impact on SMBs and, where exemption is not appropriate, not considering whether impacts on small businesses might be disproportionate or, where they are, addressing potential mitigation of these impacts.

The RPC's assessment does not involve making judgments on policy decisions, only on the underlying evidence and analysis. It is not in the RPC's remit to judge policy decisions of exempting/not exempting small businesses. The RPC's focus is on ensuring that departments meet the SaMBA requirements set out in the better regulation framework guidance; in particular through providing a proportionate level of analytical quality and evidence underpinning their assessment of impacts on SMBs.

What should a SaMBA address?

The default position is to exempt SMBs from the requirements of new regulatory measures (see figure 1 below). In some cases, it might be possible to achieve a large part of the intended benefit even if smaller businesses are exempted – for example where larger businesses account for much of the intended regulated activity and/or where this activity accounts for a large part of the detriment the regulation seeks to reduce. If, after assessment, it is concluded that the measure should apply to SMBs, departments should consider whether there are disproportionate impacts on SMBs and, if so, whether and how costs could be mitigated. The key stages of a SaMBA are illustrated below.

Figure 1: Flow chart of key stages in a SaMBA



Step 1: Exemption

Exemption as default

The better regulation framework guidance states (paragraph 2.3.3): "*The default option is to exempt small and micro-businesses from the requirements of new regulatory measures*." If an SMB exemption is not applied, and there are disproportionate impacts on SMBs, mitigation options must be considered. Departments should consider, early in the policy-making process, whether exemption or mitigation should be applied for SMBs.

In the case below, the department applies a full exemption to SMBs because nearly all of the policy benefits would still be achieved.

Legislation to require energy suppliers to provide key, personal information on consumer bills in a machine readable format (RPC13-DECC-1962) [final stage IA]

This measure required energy providers to place a 2cm x 2cm machine-readable image, such as a bar code or a quick response code, on all domestic retail consumers' paper energy bills. When scanned by a generic reader, this image would provide access to 12 key pieces of consumption data in a format that is easy to read.

The department's original IA did not provide sufficient evidence that the objectives of the proposal could not be achieved if SMBs were exempted, given the very small market share of these businesses. On submission of a revised IA, the SaMBA provided good quantitative analysis, indicating that 10 energy suppliers are SMBs, and the total market share of these suppliers is estimated to be around 0.2%. SMBs are, however, expected to bear 3.2% of the costs associated with the measure – around £120,000 in total. Given that SMBs hold a market share of only approximately 0.2%, but the costs imposed on them are considerably higher at 3.2%, the impact on SMBs could be seen as disproportionate.

Given the very small market share of small and micro businesses, a full exemption was applied because the vast majority of the policy benefits could, nevertheless, be achieved.

What is meant by 'a sufficiently large part of the intended benefits' in figure 1?

There is no particular threshold for the proportion of benefits that would be lost which, if exceeded, would justify not applying an exemption. Ultimately, a decision on what does, or does not, constitute a 'sufficiently large part of the intended benefits' is a policy judgment.

Exemption does not generate an automatic green-rated RPC opinion

It should be noted that a SaMBA that recommends an exemption, or mitigation measures, is not necessarily fit for purpose. There may be instances where exemption could be counter-productive or significantly disadvantageous. This could be where, for example, small businesses are beneficiaries of the proposal, or with regulation concerning public safety/health, consumer protection or the provision of public goods, and the evidence and analysis in the SaMBA has not addressed these potential impacts.

Another possible reason why exemption could be rejected is because of undesirable dynamic or adverse competition effects, for example where business migrates to smaller firms if they are exempt from requirements. If this is likely to be the case, departments should provide an assessment of the likelihood of such effects, which will depend on the nature and structure of the market.

Step 2: 'Disproportionate burdens'

The economic intuition behind SMBs being disproportionately affected by regulation is that some costs resulting from complying with regulation are fixed, i.e. they do not depend on the output of the business. Since larger businesses operate on a greater scale, such fixed costs are likely to be a smaller proportion of their overall costs. An identical increase in fixed costs in absolute terms will, therefore, translate into a larger relative increase in costs for SMBs. For example, understanding, and becoming familiar with, the requirements of a new regulatory measure might well be proportionately more burdensome for a micro business than for a larger business employing a regulation manager. SMBs may require more time and resource to become familiar with the requirements of a proposal, which may involve developing new processes, training staff and IT changes. Please see the RPC 'implementation costs' short guidance note for more information.

The RPC recommends that departments consider both the increase in absolute, and relative, costs to business in assessing whether SMBs are affected disproportionately. The working assumption applied by the RPC is that small businesses are likely to be disproportionately affected by regulation, unless the evidence in the SaMBA shows otherwise.

Annex 1 includes examples of SaMBAs that addressed this issue by estimating costs and benefits to small and micro businesses.

Step 3: Mitigation

If an exemption is not applied and there are disproportionate burdens on small businesses, departments must consider mitigation of the burdens. Table 1 shows a list of potential mitigation options. This list is not exhaustive; if departments consider other mitigation options to be more appropriate for a particular proposal, they can be presented.

Table 1: List of potential mitigations for SaMBA

Full exemption (default)	A large proportion of the intended benefits of the measure can be achieved without including small and micro businesses in scope of the regulation.
Partial exemption	Exempt small and micro businesses from specific requirements of the regulation (e.g. warnings to businesses rather than applying sanctions where non-compliance is identified).
Extended transition period	Businesses of a defined size are given a longer period of time to comply compared to larger businesses.
Temporary exemption	Exempt small businesses for a period of time where immediate compliance would harm their business (e.g. where a product needs to be redesigned).
Different requirements by firm size	Could have less onerous or less frequent inspection regimes for small businesses; require small businesses to have only to register rather than be fully licensed.
Information	Provide tailored information, advice and training to small businesses.
Financial aid	Small businesses can obtain re-imbursement of compliance costs.
Opt-in and voluntary solutions	Businesses below a certain threshold can voluntarily opt-in to the regulatory regime or participate in industry-led voluntary schemes.

The case below considers the impact of the measure on SMBs and applies some mitigation to SMBs to offset the disproportionate cost imposed on them.

> **Strengthening the regulator's assessment and enforcement of operator competence in the waste sector (RPC-4122(2)-DEFRA) [final stage IA]**
>
> The proposal sets out to address the problem of seriously mismanaged waste sites by improving the assessment and enforcement of four elements of operator competence in the waste sector.
>
> The department identified that approximately 40 per cent of waste site operators can be classified as SMBs, the exclusion of SMBs would lead to a significant loss in the benefits of the policy and the negative environmental and social effects associated with poor performing SMBs would not be mitigated. The department, therefore, does not consider an exemption for SMBs as appropriate and proportionate. The department notes that the permitting process already takes the size and scale of operators into account. The IA includes several mitigation methods including allowing small operators to produce management systems proportional to their size and permitting them to gain lower cost technical and financial competence qualifications adapted to their size and the risk associated with their operation.

Evidence and analysis checklist tool – suggested methodology for measuring impacts

The RPC has produced, in collaboration with BRE and in consultation with departments, a five step 'checklist' tool for a 'high-quality' or 'best practice' SaMBA (see table 2). Departments do not necessarily have to complete all steps/boxes. For example, there is no absolute framework requirement to provide separate quantitative analysis for micro-businesses (although any significant differential impacts within SMBs should be considered and justification for why no further analysis is necessary provided). The SaMBA will not be red-rated by the RPC for not adhering exactly to the 'checklist'; it should be viewed as a tool that will help provide for a high-quality SaMBA. Where departments do not consider the steps/boxes in the checklist to be appropriate, they should explain why their approach provides a more effective identification and assessment of impacts on SMBs.

Table 2: Suggested checklist tool for a high-quality SaMBA

Have you considered…	for micro businesses?	for small businesses?
Into what sector and/or sub-sector the affected businesses fall		
Number of businesses in scope of the regulation		
Market share of businesses in scope/other relevant metrics		
Impact on businesses (do these impacts fall disproportionately on small and micro businesses?)		
Appropriate exemption or mitigation measures for businesses (see figure 1 above)		
Note: If departments demonstrate at the 'number of businesses' stage that no small or micro businesses are affected, or are likely to be in the (near) future, then the SaMBA will be sufficient, and 'impact on businesses' and 'appropriate mitigation for businesses' may not be required. If it is proportionate to do so, all five steps should be completed separately for small and micro businesses. If this is not completed, appropriate justification should be provided, or at the very least an assessment of the number of small and micro businesses in scope of the measure, and a narrative provided on differences of impact between micro and small businesses.		

Once this information has been gathered, departments can use the data to consider key tests for exemption/mitigation:

a. **'Policy cost'** of exempting small and micro business. Departments should provide an assessment of how much of the policy objective would be compromised by applying exemption/mitigation to small businesses. (This is equivalent to the assessment of whether a "sufficiently large part of the intended benefits from the regulation maintained, if an exemption is applied" in figure 1); and
b. **Impacts of (not) exempting small and micro business**. Departments should provide an indication of how much of the overall costs to business they expect to fall on SMBs. Even if the proportion of costs falling on SMBs is the same as that falling on larger businesses, fixed costs can mean that the cost are disproportionately burdensome for SMBs. See the earlier section on 'disproportionate burdens'.

As indicated above, the RPC considers the analysis and evidence to support a decision to exempt or not exempt SMBs, rather than the decision itself, which is a policy choice.

The case below estimates the market share of SMBs in scope and the proportion of the overall costs to business that are expected to fall on SMBs.

National Minimum Wage (Amendment) Regulations 2019: increases in the national minimum wage and national living wage rates (RPC-4324(1)-BEIS) [final stage IA]

This high-impact proposal increases the national living wage (NLW) and the national minimum wage (NMW) in line with the Low Pay Commission's recommendations. The IA provided a sufficient SaMBA and explained why an exemption would not appropriate.

The department estimated that SMBs employ 22 per cent of those covered by the NMW/NLW and incur approximately 34 per cent of the cost, suggesting that the burden is expected to fall proportionately more on SMBs. The department explained, however, that any exemption would not be feasible on the basis that it would significantly reduce the policy effectiveness. The department addresses how impacts are mitigated, stating that the annual NMW/NLW uplifts are fully embedded in the UK labour market and that majority of employers are aware and would be expecting the increase of the NMW/NLW. The department also states that announcement of the rates six months before policy implementation, as well as government's communications campaigns, would help SMBs to adjust to the new rates and, potentially, decrease their familiarisation cost.

RPC SaMBA expectations at consultation vs final stage

The RPC acknowledges that the micro-level data required for the analysis outlined above, especially on policy costs of exempting SMBs associated with specific measures, might be difficult to obtain or not exist at all. Any figures provided might not, therefore, be particularly robust.

However, departments should, at the **consultation stage** and where possible, provide information on the areas highlighted in table 3 below. If a department does not have all the information necessary, it should explain clearly how it aims to obtain the necessary information and use the consultation period to test its assumptions with stakeholders.

Final stage impact assessments should provide more-detailed, quantitative and robust data, where possible. If such data has not been obtained, the department must explain how it actively tried to gather the relevant information and why it was not possible or proportionate to obtain the information.

Table 3: Assessment at consultation and final stage

Consultation stage	The SaMBA should include **provisional indication of**: **1)** how much of the policy objective is sacrificed by applying a full exemption; and **2)** how much of the overall cost to business is expected to fall on small businesses (with no exemption). Since data availability might be more limited at this stage, departments may not be able to provide numerical estimates. **If data are limited at this stage, the SaMBA should include assumptions that will be tested during consultation, or at least set out how information will be obtained during consultation.**
Final stage	The SaMBA should include **broader analysis describing the likely proportion of the**: **1)** policy objective sacrificed by applying a full exemption; and **2)** overall cost to business expected to fall on small businesses. **The SaMBA should include quantitative estimates, if feasible. If no estimates are provided, departments will need to explain how they attempted to obtain the necessary information**, especially during consultation, and why these attempts had been unsuccessful.

In the consultation stage example below, the department demonstrates best practice by providing a relatively detailed SaMBA and early consideration of ways of mitigating negative impacts on SMBs.

New Build Developments: Delivering Gigabit Connections (RPC-4290(1)-DCMS) [consultation stage IA]

The department's preferred option places a dual obligation on telecoms operators and property developers to provide gigabit-capable connections to all new residential buildings. The department estimates that no small and micro telecoms operators are expected to fall in scope of this policy. However, they explained that around 42,400 construction companies will be affected by this policy and that almost all of those are SMBs. The department estimates that the average annual cost faced by SMBs to be between £3,900 and £4,700.

Given the importance of SMBs in delivering the policy objective, the department explains that a full exemption would not be appropriate. The IA, however, considered several mitigation methods, including full exemption, partial exemption, extended transition period, temporary exemption, different requirements by firm size, information, financial aid, opt-in and voluntary solutions. The department explained that these methods are likely to reduce a large part of the intended benefits of the proposal and, therefore, may not be appropriate. The RPC welcomed the Department's commitment to exploring some of these mitigation methods further during consultation. Furthermore, the department has also listed a number of ways SMBs could choose to mitigate costs, including the use of government funding targeted at small businesses information sharing and education.

Assessment of impacts on small and micro business even when a SaMBA is not required

A SaMBA is not required by the better regulation framework for *de minimis* measures or regulator BIT assessments**.** Nevertheless, it is good practice to make a proportionate assessment of impacts on small and micro businesses (as part of an assessment of any significant distributional impacts).

Although not required for a BIT EANDCB validation, the regulator's assessment below addressed costs and benefits to small and micro businesses.

Client money and unbreakable deposits (RPC-4254(1)-HMT-FCA) [EANDCB validation]

Unbreakable terms were introduced so that investment firms can react to risks by withdrawing and relocating client money. However, the FCA received feedback that this rule was making it difficult for some investment firms to deposit client money with banks, due to the bank's liquidity coverage ratio requirements. This proposal extends the unbreakable terms for FCA-regulated firms from 30 days to 31 and 95 days.

The regulator estimates that, as of July 2017, there are 596 affected firms, 124 of which are classified as small businesses. The proposal is expected to yield benefits to firms in the investment sector, and the regulator does not expect that extending the permitted unbreakable term will impose significant costs on firms. However, the FCA has provided a clear breakdown of the transition and ongoing costs and benefits of the extension and explained how they are expected to impact both small and large firms within the investment sector. For example, the regulator estimates that the one-off cost associated with client disclosure will be £250 for small and medium firms and £1,500 for CASS large firms.

Contacts and queries:

For further information about completing the SaMBA, please e-mail regulatoryenquiries@rpc.gov.uk. The RPC welcomes pre-submission meetings with departments.

Annex 1

Examples of SaMBAs that estimated costs and benefits to SMBs

Departments should include an assessment of costs and benefits for SMBs in their SaMBAs, if it is proportionate for them to do so. The estimation should include the impacts of the proposal on SMBs and whether these impacts fall disproportionately on SMBs. The case below identifies the number of small and micro firms affected, the market share of SMBs in scope and estimates the cost incurred by these firms.

Standardised packaging of tobacco products (RPC12-DH-1229(4)) [final stage IA]

This is a high-impact proposal; the objective of which is to improve public health by discouraging the use of tobacco products through the standardisation of tobacco packaging. Although the department explains that the firms involved in the manufacturing and branding of tobacco packaging are large businesses, a significant proportion of tobacco sales are made through SMBs. The department estimates that there are 49,800 small businesses selling tobacco in England (comprising convenience shops and petrol forecourts) and that they comprise approximately 46 per cent of the tobacco sales in the UK. This assumption suggests that there will be a profit loss of £95m to small and micro retailer's profits due to reduced tobacco sales and £42m due to downtrading (discounted over 10 years).

The department estimates that there may potentially be two impacts on SMBs: first, from the overall reduction in the quantity of cigarette and hand-rolling tobacco sales and second by the downtrading from higher priced brands to less profitable lower priced brands. Consultation responses suggest that standardised packaging is expected to decrease the demand for tobacco and tobacco-related products. The Department estimates that SMBs are expected to face reduced profits from a decline in tobacco sales, however, some of this impact could be partially offset by an increase in expenditure on non-tobacco goods. The department has indicated the number of SMBs in scope and quantified the impacts of the proposal on them. Although it was recognised that costs might fall disproportionately on SMBs, the department explained that exempting SMBs would not be appropriate as it would prevent the policy objective from being achieved.

The case below estimates the costs and benefits of the proposal for SMBs. The department explains how SMBs could benefit from the proposal at both a macro and a micro level.

Continuity of essential supplies to insolvent businesses (RPC13-BIS-3264) [final stage IA]

When a business enters insolvency, suppliers may invoke a termination clause in their contract and withdraw their supply. Where those supplies are essential to the continuation of the business, this can have an adverse impact on the likelihood of a successful rescue of the business and on the amount returned to creditors. These essential suppliers may also threaten to withhold supplies or services unless a 'ransom' payment is made. This causes a transfer from the body of creditors of the insolvent business to the essential supplier, reducing the likelihood of a business rescue and reducing returns to the wider body of creditors.

The IA provides detailed quantitative analysis on the number of small and micro businesses affected, the reduction in benefits from exempting small and micro businesses, and the costs to small and micro businesses of the proposal. It explains that small and micro businesses can be expected to benefit from the policy at both a macro and micro level, through the following impacts:

- Improved returns to unsecured creditors generally (nearly 90 per cent of which are small or micro businesses) of £46.69 millions. This benefit would be significantly reduced in the event that small and micro business suppliers were excluded from the scope of the policy, with any benefits to excluded suppliers occurring as a transfer from other businesses (up to 99 per cent of which are likely to be small or micro businesses).
- Enhanced prospect of business rescue for small and micro businesses that are dependent on supplies and that are enabled to continue trading.

The department concludes that exempting small and micro businesses would significantly undermine the rationale for the policy and its benefits – and particularly the benefits to small and micro businesses. The SaMBA explains that specific guidance and information for small and micro businesses will be made available to mitigate potentially disproportionate familiarisation costs. The department also explains that it will engage with representative bodies of suppliers affected.

The department explains that the impact on small and micro businesses will be monitored and reported on as part of the post-implementation review.

The case below provided more information on the number of SMBs in scope and quantified the impacts on these businesses.

Gaming machines and social responsibility measures (RPC-4137-DCMS) [final stage IA]

This is a high-impact policy. This SaMBA has indicated the number of small businesses affected by the regulation and quantified the impacts on small businesses. The department provided information from the Gambling Commission, which indicates that the number of small and micro businesses affected by the change amounts to approximately 1.3 per cent of the sector. Additionally, the department now provides estimated quantified impacts for small and micro businesses of each of the appraised options. Furthermore, the department explains clearly why exemptions for small and micro businesses are not considered appropriate on the basis that the policy objective would not be achieved; there is a high likelihood that there would be significant substitution because there is no difference between B2 gaming machines offered by large operators and those in small or micro businesses.

Besides extending the transition period for small businesses, the department provides a clear explanation as to why various potential measures to mitigate the impact of the policy on small and micro businesses have not been taken forward.
Whilst there is a large amount of uncertainty in the data, the impact assessment provides an appropriate and proportionate estimate of the costs to business of the policy.