Title: The Capital Requirements Regulation (Amendment) (EU Exit) Regulations 2021 **SI No:** Click here to enter text. **Other departments or agencies:** None **Contact for enquiries**: Jos.Kelly@hmtreasury.gov.uk	De minimis assessment **Date: 17/03/2021** **Type of regulation: EU** **Date measure comes into force:** **26/06/2021**
Cost of Preferred (or more likely) Option: £0	**Equivalent Annual Net Direct Cost to Business per year** (EANDCB in 2019 prices) £0

1. What is the problem under consideration? Why is government intervention necessary?

The retained Capital Requirements Regulation (CRR) makes provision, through Articles 493 and 498, to exempt commodities dealers from specific prudential requirements. These exemptions, relieve commodities dealers of three notable obligations:

1. To hold regulatory capital equal to at least 8% of total risk exposures;
2. To calculate and report exposures to any individual counterparty equal to or greater than 10% of a firm's eligible capital; and third,
3. A prohibition from having exposures of more than 25% of eligible capital or EUR 150 million to a counterparty or group of counterparties.

Both the EU and the UK are set to introduce separate prudential regimes that are tailored specifically to non-systemic investment firms, including commodities dealers. This will replace the CRR for these firms. The EU's regime will be called the Investment Firms Regime (IFR) and is due to be introduced on 26 June 2021. It will apply to all EU investment firms, including commodities dealers. The UK's equivalent regime for investment firms including commodities dealers will be called the Investment Firms Prudential Regime (IFPR). It will not be introduced until 1 January 2022, and if government did not intervene through this SI, this would create six months of disruption for UK commodities dealers.

The EU amended the CRR's exemption provisions for commodities dealers to align with the planned introduction of the IFR. Consequently, EU commodities dealers are not required to comply with the provisions of the CRR before the IFR applies to them. Because of the UK onshoring the CRR, these EU amendments apply in UK law.

Without amendment, Articles 493 and 498 of the CRR will require UK commodities dealers to comply with the prudential requirements of the CRR set out above between 26 June and 31 December 2021. They would then need to comply with a different prudential regime, the IFPR, from 1 January 2022. Such a development would amount to a significant regulatory burden for UK commodities dealers, which would accrue no material benefit to the wider regulatory system given the short period of compliance. This would also impinge on competitiveness, as UK commodities dealers would be subject to a more onerous regime for six months when EU counterparts – which would be subject to the tailored IFR – would not.

The problem under consideration concerns EU retained law that can only be amended via legislation. HMT considers that the retained EU law in question does not operate effectively in the UK, because of the negative impact it would cause to commodities dealers, and that it's right and necessary that the UK government intervenes to effect the required amendments to EU retained law.

2. What are the policy objectives and the intended effects?

The objectives of this SI are to ensure that the legal status quo persists between 26 June-31 December 2021 for the prudential requirements that apply to UK commodities dealers and that the UK's regulatory regime operates effectively after EU exit. More specifically, these objectives will see commodities dealers remain exempt from the provisions listed in Question 1 up to and including 31 December 2021:

- 1. The obligation to hold regulatory capital equal to at least 8% of total risk exposures
- 2. The obligation to calculate and report exposures to any individual counterparty equal to or greater than 10% of a firm's eligible capital
- 3. The prohibition of incurring exposures of more than 25% of eligible capital or EUR 150 million to a counterparty or group of counterparties

Achieving these objectives will give UK commodities dealers firms greater certainty on their near-term, future regulatory obligations. They will also minimise undue regulatory burden for commodities dealers, by preventing them from having to comply with new prudential requirements for just over six months, before the IFPR applies to them.

3. What policy options have been considered, including any alternatives to regulation? Please justify preferred option

The main alternative policy option was the 'do nothing' option, as any other positive action would be nugatory and / or counterproductive ahead of the planned introduction of the more proportionate and tailored IFPR. Alternative positive action would be nugatory and counterproductive because work to apply commodities dealers to a more tailored prudential regime has been done as part of the creation of the IFPR, and carrying out the same work would take resources away from more productive activities. Furthermore, any alternative positive action risks impinging the rollout of the IFPR.

Doing nothing would see UK commodities dealers lose their exemption to the own funds requirement and large exposure limits set out in Articles 493 and 498 of the CRR between 26 June and 31 December 2021. This would foist a significant regulatory burden upon commodities dealers, and it would penalise them – through the need to hold higher regulatory capital and use more internal regulatory resource – without bringing about any obvious wider benefit.

The preferred policy option will avoid these pitfalls and will achieve the policy objectives set out in question 2.

4. Please justify why the net impacts (i.e. net costs or benefits) to business will be less than £5 million a year.

This legislative amendment seeks to maintain the legal status quo for UK commodities dealers, such that they remain exempt from certain CRR provisions until 31 December 2021. But, if this amendment were not made, then the regulatory costs to each UK commodities dealer would be significant and these impositions would not bring about any wider benefits.

This table shows the one-off incremental cost to UK commodities dealers in 2019 prices that would occur if the UK government didn't make the relevant amends to EU retained law and these firms were subject to the CRR between 26 June and 31 December 2021:

Type of investment firm	Total cost to small commodities dealers (£)	Total cost to mid-sized commodities dealers (£)	Total cost to large commodities dealers (£)	Total cost to all (small, mid-sized and large) commodities dealers
Commodities dealers	£1,110,000.00	£1,610,000.00	£1,210,000.00	£3,930,000.00

The costs are based on the latest and most relevant data about the application of the CRR to UK investment firms from 2013, which have been adjusted for inflation using the Bank of England inflation calculator. The Financial Conduct Authority's Consultation Paper shows that in 2013 the estimated incremental one-off cost of compliance with the CRR for investment firms was £20,000 for small firms, £155,000 for mid-sized and £350,000 for large investment firms (see page 66).

The breakdown in size of UK commodities dealers comes from recent FCA internal data requests, which shows that there are around 56 regulated commodities dealers in the UK. For the purposes of this calculation, we rounded this number up to 60. And as this FCA data itself isn't broken down by size, we applied the same breakdown in size of UK investment firms subject to the CRR in 2013 to estimate that there are currently 48 small, 9 mid-sized and 3 large commodities dealers in the UK.

Sensitivity analysis

Increase in number of larger firms: as the cost of compliance is the least for small firms and the most for large firms, if the proportion of small, mid-sized and large commodities dealers has changed significantly since 2013, then the total cost to UK commodities dealers could be higher.

Additional rules: since 2013, UK investment firms have faced additional, incremental regulatory costs as a result of new CRR rules. These costs may see commodities dealers face higher compliance costs in the counterfactual.

Overall, we do not believe these sensitivities would result in more than a 25% increase in total costs i.e. enough to push the total cost above the de minimis threshold, particularly given that the calculation to derive the total cost assumed the existence of more commodities dealers than current data suggest.

5. Please confirm whether your measure could be subject to call-in by BRE under the following criteria. If yes, please provide a justification of why a full impact assessment is not appropriate:

a) Significant distributional impacts (such as significant transfers between different businesses or sectors)
   No.
b) Disproportionate burdens on small businesses
   As set out above, this legislative amendment maintains the legal status quo, resulting in no burden for businesses, including small businesses.
c) Significant gross effects despite small net impacts
   No.
d) Significant wider social, environmental, financial or economic impacts
   No.
e) Significant novel or contentious elements
   No.

Sign-off for de minimis assessment: SCS

I have read the de minimis assessment and I am satisfied that it represents a fair and proportionate assessment of the impact of the measure.

SCS of Green and Prudential

Signed: Fayyaz Muneer Date: 17/03/2021

SCS of Better Regulation Unit

Signed: Linda Timson Date: 17/03/2021

<u>Sign-off for de minimis assessment: Minister</u>

I have read the de minimis assessment and I am satisfied that it represents a fair and proportionate assessment of the impact of the measure.

Signed: John Glen Date: 22/03/2021