Energy UK

The voice of the energy industry

Commodities trading – No deal Brexit

This information is meant for guidance only. You should consider whether you need separate professional advice before making specific preparations.

A no deal Brexit may impact trading in commodities for firms located in the UK and in the EU-27 Member States. Whilst the UK, through the EU (Withdrawal) Act 2018, is retaining and replicating most elements of EU legislation, the scope of certain EU legislations could alter with the UK becoming a third country.

The main impacts are linked to financial market legislation – EMIR and MiFID in particular – as well as REMIT. For those trading electricity, there may also be impacts from the decoupling of day-ahead markets in GB from the rest of the EU. The carbon markets in the UK will be replaced by a carbon tax and installations will no longer be subject to the EU ETS. Lastly, UK firms especially those trading natural gas in certain jurisdictions in the Union will have to consider if their authorisations, licences and contracts may be revoked when the UK will leave the European Economic Area (EEA).

1. Financial Market Regulation

For firms and traders trading commodities, some of the most important changes in a no deal Brexit will relate to their status and obligations under the European Market Infrastructure Regulation (EMIR) and the EU Markets in Financial Instruments Directive (MiFID II). Whilst this may not directly impact UK firms, it could impact their counterparties' willingness and/or ability to trade with them in the same way as before.

In a no deal scenario, UK based trading platforms would become third country venues under EU legislation and this will affect those entities subject to EU legislation.

1.1 EMIR

Under EU EMIR, unless an equivalence decision is made vis-à-vis UK regulated markets by the European authorities, derivatives traded on UK regulated markets that were categorised as Exchange Traded Derivatives ("ETDs") before Brexit, will be re-categorised as OTC derivatives ("OTCDs") after Brexit, and this alters the obligations of those trading these derivatives. Areas of consideration include reporting, calculation of the EMIR clearing threshold and any changes that may result from a change in EMIR status if that threshold is breached. Changes in destination of reporting of transactions may also impact businesses in UK markets.

The EU has proposed temporary equivalence for Clearing houses (CCPs) and central depositaries services (CDSs), but not currently for UK regulated markets. Trade repositories (TRs) must also be approved if located in a third country.

1.2 MiFID

Under EU MIFID, firms may need to reconsider the delineation between so called physical and financial products. The retention of the C6 'REMIT' carve out for physically settled gas and power derivatives traded on an OTF is dependent on the OTF being authorised in the EU. Many London based OTFs are relocating part or the entirety of their business to EU jurisdictions.

Another change to the EU MiFID legislation will come in the reduction in market size used in the ancillary activity exemption test by non-financial commodity firms. For some commodities the removal of UK based venues and transactions from the market size could be substantial and affect their right to the exemption. The impact of this reduction will be gradual given the 3-year calculation period.

2. REMIT (see REMIT information sheet)

There will be no changes in the obligation of firms relating to the market integrity elements of REMIT, changes may be needed in the areas of registration and reporting.

Firms currently registered with a UK regulatory authority will need to register with an EU NRA if they wish to continue trading in a EU27 market post Brexit. For EU27 firms wishing to continue trading in the UK, no Sre-registration is needed.

3. Electricity Trading

Under a no deal Brexit, the GB electricity market will be decoupled from the EU27 markets. This will impact the way in which capacity is allocated on the GB interconnectors on day ahead basis as well as the participation of National Grid in certain future EU wide balancing initiatives.

In the day-ahead timeframe, capacity on the GB interconnectors will revert to the pre-February 2014 explicit capacity allocation methodology and nomination of capacity.

Another consequence of the decoupling will be that a single cleared price for GB in the day-ahead timeframe will no longer be guaranteed. The two GB NEMOs will lose their status and the legal framework underpinning market coupling will not exists after no deal. The prices for each exchange will be derived from the bids and offers posted on each exchange separately.

4. Carbon Markets (see carbon pricing information sheet)

In the event of a no-deal Brexit, UK installations will no longer be subject to the EU Emissions Trading Scheme and will move to a carbon tax regime.

The UK government has suspended allowances auctions for 2019 until further notice.

Post-Brexit, UK account holders will no longer be able to access the EU registry of emission allowances unless they have been moved to an account in another EU jurisdiction.

Things to consider

EU-27 firms trading on UK trading platforms	EU27 firms trading on UK exchanges need to explore how their trading might be affected: recategorisation of ETDs into OTCDs, understand whether there is a need to amend existing contracts and, if affected, whether they should move their trading activities to EU recognised platforms if available.
EU-27 exchanges participation in UK markets	Passport rights will no longer apply to MiFID II EEA market operators seeking to participate in UK markets. They will need to apply to become a recognised overseas investment exchange (ROIE).
EMIR clearing threshold – UK and EU firms	Both EU and UK firms will have to consider whether their clearing status under EMIR might change in a no deal scenario. Currently firms with OTC derivative contracts valued above a certain limit (clearing threshold) must comply with stricter risk mitigation rules under EMIR. As UK exchanges will no longer be recognised by the EU, contracts traded on UK exchanges would be recategorised as OTC. As a result EU firms will need to include such trades in their calculation with regards to the clearing threshold. Similarly, and unless the UK starts recognising EU regulated markets, under UK EMIR, contracts traded on EU exchanges would be considered OTC and UK firms would need to include them in calculating whether they exceed the clearing threshold under UK EMIR.

Intragroup exemption under EMIR	Companies may no longer be able to rely on the intragroup exemption under EMIR which exempts from EMIR's clearing obligation trades between two EU members of a group, or between an EU company and a company in a third-country which benefits from an equivalence decision. As a result, certain EU companies could be required to clear intragroup trades with UK companies. For UK companies, the position is different. Under UK EMIR, the government has proposed a temporary exemption regime, which will allow UK companies that relied on an intragroup exemption prior to exit day, to continue to rely on this exemption after Brexit.
Central Counterparties	The European Commission has adopted an implementing decision which will allow UK CCPs which were authorised prior to Brexit to continue providing clearing services after Brexit. UK CCPs would therefore continue to be recognised by the EU for the purposes of EMIR. Under EMIR, certain firms are required to clear their OTC derivatives with a CCP which is authorised or recognised by the EU. The vast majority of derivatives are currently cleared through UK CCPs.
Ancillary activities exemption under MIFID II	In a no deal scenario, firms will need to consider their status under MiFID II, especially those currently relying on the ancillary activities exemption which allows firms trading commodities derivatives on own account largely for the purposes of hedging to remain outside the regulatory scope of MiFID II. EU firms would no longer consider trading done on UK venues when considering the size of their own speculative positions. This could affect their suitability under the market share test given that almost all trading in certain asset classes, such as coal, oil and metal, takes place in the UK. Under UK MiFID II firms must continue to consider their EU trading in their "market share test". Most UK firms which currently easily pass the market share test are likely to continue to do so in a no deal Brexit.
Electricity trading	Interconnector owners/operators will need to continue to work with their stakeholders and regulators to prepare alternative trading arrangements and updated rules. UK market participants will need to register under REMIT with an EU regulatory authority for the purposes of market monitoring to avoid a disruption to cross-border trade, trade within EU wholesale energy markets, or trade within the Single Electricity Market. In Northern Ireland, electricity market participants should continue using the SEM processes and arrangements but should be aware of the risk that the SEM may not be able to continue, in which case government and the Northern Ireland Utility Regulator will take action to seek to ensure continued security of supply and market stability. Market participants should also check the status of contracts, and licences held in EU Member States, which may be impacted.

Trading other commodities	UK firms trading and shipping commodities, especially natural gas, in the EU will have to consider if their authorisations, licences and/or shipping contracts will still be valid when the UK will leave the European Economic Area (EEA). This needs to be assessed on a case by case by these trading firms. This may lead to the need to amend existing contracts and/or to apply for new authorisations or licences through EEA based legal entities.

Relevant documents/information

Preparing for Brexit

Preparing your firm for Brexit

The temporary permissions regime for inbound passporting EEA firms and funds – our approach

Brexit: European Commission implements "no-deal" Contingency Action Plan in specific sectors

Withdrawal of the United Kingdom and EU rules in the field of markets in financial instruments

Withdrawal of the United Kingdom and EU rules in the field of post-trade financial services

Trading electricity if there's no Brexit deal

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