

Stellungnahme

BDEW Response ESMA Call for Evidence on Position Limits un- der MiFID II:

Berlin, 9. Juli 2019

#	ESMA Question	BDEW response
1	<p>In your view, what impact, if any, did the introduction of position limits have on the availability and liquidity of commodity derivative markets? What are in your views the main factors driving this development, e.g. the mere existence of a position limit and position reporting regime, some specific characteristics of the position limit regime or the level at which position limits are set? Please elaborate by differentiating per commodity asset class or contract where relevant and provide evidence to support your assessment.</p>	<p>BDEW has not identified any significant impact on liquidity in the current 18-month experience yet. The introduction of position limits has not disrupted commodity markets in a major way. However, the short experience period may be insufficient to draw firm conclusions.</p>
2	<p>Have you identified other structural changes in commodity derivative markets or in the underlying markets since the introduction of the MiFID II position limit regime, such as changes in market participants? If so, please provide examples, and where available data, and differentiate per commodity derivative asset class where relevant.</p>	<p>BDEW has not identified any structural changes in commodity derivative markets following the introduction of position limits, except from the transfer of about 250 contracts from the UK-based trading venue ICE Futures Europe to ICE Futures US. The underlying of these contracts were globally traded oil-related products and market participants included both EU and non-EU firms.</p>
3	<p>Do you consider that position limits contribute to the prevention of market abuse in commodity derivatives markets? Please elaborate by differentiating per contract, per commodity asset</p>	<p>Position limits are an effective tool to prevent only certain types of market abuse, such as abuse of dominant position and cornering the market. Even though article 57.1 (a) of MiFID specifies that one of the objectives of position limits is to prevent market abuse, BDEW does not believe this should be the main focus of the regime.</p>

	classes or contract where relevant and provide evidence to support your assessment when available.	BDEW considers the Market Abuse Regulation as an effective and comprehensive tool to prevent market abuse.
4	In your view, what impact do position limits have on the orderly pricing and orderly settlement of commodity derivative contracts? Please elaborate by differentiating per asset class or per contract where relevant and provide evidence to support your answer when available.	BDEW members have not noticed any significant impact of position limits on orderly pricing and orderly settlement in commodity derivative markets, even though the current 18-month experience may be insufficient to draw firm conclusions.
5	More generally, and beyond the specific items identified above, what would be your overall assessment of the impact of position limits on EU commodity derivatives markets since the application of MiFID II?	<p>BDEW believes that, with the exception of the limits applied to new and illiquid contracts, the position limit regime introduced by MiFID II is generally working well. While the implementation of internal controls and monitoring tools has been burdensome for market participants, its day-to-day functioning has no adverse impact on the liquidity and orderly functioning of commodity derivative markets. BDEW advises against proposing any kind of strengthening of the system as this would potentially endanger the functioning and liquidity of the wholesale commodity markets. A further simplification of the system would be welcomed to reduce the current compliance and monitor burden for all concerned parties, incl. firms, exchanges and NCAs, for example by focusing the system on “core” (benchmark) contracts.</p> <p>As for the new and illiquid contracts, the limits applied under article 15 of RTS can in certain cases prevent the development of the market for contracts and can incentivise trading venues to locate these contracts outside of the European Union.</p>
6	Do you consider that position management controls have an impact on the liquidity of commodity derivatives markets? If so, please elaborate, differentiating per	BDEW did not notice any significant impact on liquidity of commodity derivative markets.

	commodity derivative trading venues or contract where appropriate.	
7	Do you consider that position management controls adopted by commodity derivative trading venues have a role on the prevention of market abuse? If so, please elaborate, differentiating per commodity derivative trading venues or contract where appropriate.	As argued in Question 3 above, BDEW believes there are better tools to prevent market abuse, as position limits are effective to prevent only certain types of market abuse.
8	Do you consider that position management controls adopted by commodity derivative trading venues have a role on orderly pricing and settlement conditions? If so, please elaborate, differentiating per commodity derivative trading venues or contract where appropriate.	BDEW believes that position management controls are not a critical element in determining orderly pricing and settlement conditions as by their nature are used only in exceptional circumstances. Exchanges are best placed to determine how to implement position management controls and when it is necessary to trigger them.
9	If you are a commodity derivative trading venue, please explain how you have been exercising your position management controls since MiFID II application. In particular, how frequently did you ask further information on the size or purpose of a position, on beneficial owners or assets and liabilities in the underlying commodity under Article 57(1)(b) of MiFID II, require a person to terminate or reduce a position under Article 57(1)(c) of MiFID II, require a person to provide liquidity back into the market under Article 57(1)(d) of MiFID II or exercise any of your additional	N/A

	position management controls?	
10	Do you have any general comment on the position limit regime and associated position reporting introduced by MiFID II?	<p>As argued in Question 5, BDEW believes that, with the exception of the limits applied to new and illiquid contracts, the position limit regime introduced by MiFID II is generally working well.</p> <p>BDEW suggests 3 adjustments:</p> <ul style="list-style-type: none"> - As proposed by ESMA in Question 13, we recommend a refocus of the position limit regime to benchmark contracts. If that for some reasons can not be achieved, we recommend to change the regime for new and illiquid contracts. - Transfer of limit monitoring to the stock exchanges: it is inefficient if every market participant himself has to set up a process to monitor the position limits. - One centrally available overview of the currently valid limits would be very helpful operationally. Otherwise, we would not recommend any other changes or overhaul of the system.
11	In your view, how will EU commodity derivatives markets be impacted by the UK leaving the EU? What consequences do you expect from Brexit on the commodity derivatives regime under MiFID II?	<p>BDEW does not expect any major impact on the position limit regime by the Brexit.</p> <p>The main impact on commodity derivative markets, as noted by ESMA in paragraph 14 of this Call for Evidence, is linked to the fact that the liquidity in many commodity derivatives (namely oil, coal, metal and EUAs) is concentrated on UK trading venues, with very low levels of activity in the EU27. This will have significant consequences on the market size test governing the ancillary activity exemption for own-account traders in commodity derivatives and emission allowances. While this may take time to impact market participants (as the calculation is a three-year average and activities in the UK will be included until at least 31 October 2019), we urge ESMA to start to consider solutions, including the increase of the threshold for these asset classes or a redesign of the test in Level 2 legislation.</p> <p>The lack of recognition of UK exchanges as equivalent under EMIR would put EU27 Non Financial Counterparties (NFC) at a disadvantage as their activity on UK exchanges would count towards the so-called EMIR clearing threshold and may cause some of them to breach it.</p>

		Therefore, we still urge the recognition of UK commodity exchanges under Art. 2a of EMIR.
12	Taking into consideration the intended purposes of position limits, do you consider that they deliver the same benefit across all commodity asset classes and across all types of commodity derivatives? Please explain.	BDEW believes that the application of position limits on a large number of contracts is redundant. Therefore, BDEW proposed a more focused scope of application before the entry into force of MiFID II. See also answer to Question 13.
13	Would you see benefits in limiting the application of position limits to a more limited set of commodity derivatives? If so, to which ones and on which criteria?	<p>BDEW agrees with the view of ESMA that there “could be merits in limiting the application of MiFID II position limits II to a more limited set of important, critical (benchmark) commodity derivative contracts”. BDEW argues that such a refocus of position limits on a limited set of important “core” or “benchmark” contracts is the best approach to benefit from the existence of position limits. Granting National Competence Authorities (NCAs) greater flexibility in setting the limits - including the decision to not set any limits - would allow for this more efficient approach without the need for a radical overhaul of the position limit regime. Otherwise, we would recommend no further changes to the system after such a short period.</p> <p>This refocus would make the system more efficient, mitigate non-intended consequences and reduce the compliance burden for all concerned parties (market participants, trading venues, NCAs/ESMA). Most importantly, such an approach would avoid stifling the development of new and illiquid products. Furthermore, the refocus on key benchmark contracts is justified as the price formation mainly occurs in such benchmark products and only in so far it seems necessary and appropriate to reduce the potential threat of market manipulation and congestion during the spot month. Finally, this would create a regulatory level-playing field between the EU and US commodity markets and protect the liquidity and competitiveness of EU commodity markets.</p>
14	More specifically, are you facing any issue with the application of position limits to securitised derivatives? If so, please elaborate.	N/A

15	Do you consider that there would be merits in reviewing the definition of EEOTC contracts? If so, please explain the changes you would suggest.	BDEW does not support a review of the definition of EE-OTC contracts.
16	In your view, would there be a need to review the MiFID II position limit exemptions? If so, please elaborate and explain which changes would be desirable.	<p>BDEW urges ESMA to promote greater coordination in the implementation of exemptions from position limits across the Union. We believe that firms should be granted a hedging exemption without the imposition of a quantitative limit to this exemption. Quantitative limits create unnecessary administrative burden. The robustness of the regime and the supervisory capabilities of NCAs would be unaffected as NCAs can monitor the use of the exemption on the basis of the daily position reports.</p> <p>Moreover, ESMA should give consideration to the proposal to also allow financial firms to benefit from an exemption for positions to objectively reduce the commercial risk of the position holder or their clients. This should lead to a facilitating for banks, offering hedging services to smaller companies that do not have access to exchanges.</p>
17	Would you see merits in the approach described above and the additional flexibility provided to CAs for setting the spot month limit in cash settled contracts? Please explain.	BDEW does not see the need for changes in the existing methodologies. Regulators are already given sufficient flexibility to set spot month limits as a percentage of deliverable supply, using a higher or lower percentage on the basis of a number of intervening factors. The deliverable supply is the appropriate basis for setting limits for commodity derivatives contracts. They have a strong interlinkage with the underlying physical markets in power and gas markets, in particular when these commodity derivatives contracts are physically settled.
18	Would you see benefits to review the approach for setting position limits for new and illiquid contracts? If so, what would you suggest?	<p>There are benefits in reviewing the approach for setting position limits for new and illiquid contracts (in case there will be no refocus on benchmark contracts).</p> <p>Under RTS 21, ESMA has established a specific regime for new and illiquid contracts for the purpose of calculations of position limits. Article 15 of RTS 21, states that new contracts traded on a trading venue with a total combined interest in spot and other months not exceeding 10,000 lots over a consecutive three-month period shall be set a limit of 2,500 lots.</p>

	<p>Some NCAs have interpreted these requirements under Article 15 of RTS 21 to mean that on day 1 of a new commodity derivative, a limit of 2,500 lots would apply. In some instances, such a limit is too restrictive to allow a new contract to develop into a liquid instrument.</p> <p>Existing derogations for illiquid markets which have an open interest between 5,000 and 10,000 lots under the ESMA Q&As are welcome and should be applied by NCAs. However, they remain often not sufficient to mitigate the negative impact of disproportionately low position limits.</p> <p>In particular, once a market participant approaches the position limit, it is likely to withdraw from the market and switch to another trading venue outside of the MiFID II regime, leaving the NCA no time to adjust the limit upwards. Furthermore, in relation to newly launched contracts, it is not unusual that only one participant sits on the buy or sell side of the market, making a limit of 50% (which is the maximum allowed by the existing derogations) not sufficient to allow the market to further develop.</p> <p>BDEW supports the following approach to the application of the position limits regime to new contracts:</p> <p>ESMA should consider revisiting RTS 21 to allow a review period for new contracts (3 months, 6 months, 9 months, depending on the contract) during which no position limit is set. This would allow the concerned NCA to review the development of the contract and to determine a position limit appropriately calibrated regarding the needs of the market. This is supported by the policy objective of the MiFID II as expressed in its implementing RTS 21 which provides that “Position limits should not create barriers to the development of new commodity derivatives and should not prevent less liquid sections of the commodity derivative markets from working adequately“.</p> <p>New and nascent products normally constitute a minor share of commodity markets. Moreover, such contracts are unlikely to influence such price movements in the underlying physical commodity markets that could negatively impact consumers. Thus, the suspension of position limits for such contracts would not pose any risk to</p>
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		<p>the transparency and functioning thereof. Rather, attracting more volume to regulated venues would contribute to a more transparent trading environment.</p> <p>However, should such assessment period without limits not be possible, BDEW recommends that the current provisions are nonetheless adjusted in order to mitigate their adverse negative impact on the development of markets in commodity derivatives.</p> <p>BDEW proposes that the current de minimis limit for illiquid markets is increased to 5,000 lots to better accommodate the nature of fast growing contracts. Such an approach would ensure that the development of contracts is not curbed by an overly restrictive limit once open interest grows closer to the 10,000 lots upper range of the illiquid markets category. Additionally the overall framework becomes less dependent on unreasonably high levels of flexibility required from NCAs in terms of re-classifying markets and re-calibrating applicable limits on a near real-time basis.</p> <p>For contracts between 10,000 lots and 20,000 lots or “less liquid contracts”, BDEW proposes that the current derogation for the position limit should go up to 50% and be transformed into a default approach from which derogations could be envisaged if needed.</p>
19	<p>Would you see merits in a more forward-looking approach to the calculation of open interest used as a baseline for setting position limits? Please elaborate.</p>	<p>As argued in Question 17, BDEW does not see the need for changes in the existing methodologies. Regulators are already given sufficient flexibility to set limits as a percentage of deliverable supply or open interest, using a higher or lower percentage on the basis of a number of intervening factors.</p>
20	<p>In your view, are there other specific areas where the methodology for calculating the position limits set out in RTS 21 should be reviewed? If so, what would you suggest, and why?</p>	<p>BDEW believes ESMA and the NCAs should ensure that the same methodology to calculate open interest is applied for the purpose of setting position limits across the Union. This would allow all venues and market participants to operate in a fair and competitive landscape where the position limit regime is not creating an unequal level playing field.</p> <p>We support the use of gross open interest as the most appropriate methodology. If a member holds 5 lots long for client A and 5 lots short for client B, this position should not be netted, as the positions belong to different beneficiary owners.</p>

21	How useful do you consider the information on position management controls available on ESMA's website?	N/A
22	Do you consider that there is a need to review the list of minimum position management controls to be implemented by commodity derivatives trading venues under Article 57(8) of MiFID II? If so, please explain the changes you would suggest.	N/A

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