

To: CESR
11-13 Avenue de Friedland
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FRANCE

Subject: *comment on consultation document*, CESR's draft technical advice on the implementation of directive 2004/39/EZ on markets in financial instruments; in particular regarding energy commodities electricity and gas.

Introduction

APX is an international energy exchange operating short-term spot markets in electricity and natural gas in the Netherlands, United Kingdom and Belgium.

From the consultation document, we understand that commodities, in particular energy commodities, will fall under a directive, in order to achieve harmony with other financial instruments as well as support a "European passport" for such instruments.

Support for European passport; need to keep regulation to a minimum

APX supports the purpose of a "European passport" for energy commodities, especially from our perspective of an international energy exchange. At the same time, we feel that any regulation should be kept to a minimum as much as possible as far as this concerns commodities, in particular energy commodities. For this, there are three main reasons:

- Up till now, commodity trade or energy trade is not financially regulated in many countries. Therefore, one should be careful introducing this legislation.
- Any adverse or top-heavy regulation would have an adverse effect by pushing away the trading from regulated to unregulated paths (from exchange-based to bilateral). Trading of energy or energy derivative contracts can be done through the exchange or bilaterally, mostly facilitated by brokers. The bilateral facilities would not fall under the financial regulation, while energy exchanges would. Consequently, the exchange, being regulated, risks facing higher costs compared with bilateral trade, putting exchange trading at a disadvantage and pushing trade away from the organized and regulated markets. This should be avoided.
- As many energy markets (notably electricity and natural gas markets) tend to be illiquid partly due to incomplete liberalization and/or insufficient transportation capacity of grids, it is important not to burden those markets with regulation being detrimental to liquidity.
- Another area of attention is the interference between the financial supervision and energy supervision, in particular for goods being often called "public", notably electricity. For electricity, there is often an extensive specific legislation, and also a special supervisory authority (often called the regulator).

Exclusion of spot contracts

The document mentions the exclusion of spot contracts from the regulation. We support this, as spot trading of gas and electricity tends to be a very important tool for balancing shortages and losses for physical players, as well as optimizing the short-term dispatch of physical production capacity and storage, and supply and demand (including flexible demand reacting to shortages and prices, the so-called load management). Clearly, these types of product are not to be seen as financial instruments.

We believe, that any exclusion of spot contracts should be simple and straightforward in order to avoid lengthy procedures and discussions, possibly leading to blockades against a sound development of the energy market, and to avoid bias or unequal treatment across the European Union. The criterion of “generally settlement period” would lead to such discussions: it is often unclear what that period is, and it may vary over time as well as from country to country. We strongly prefer a certain fixed number of working days.

A certain fixed number of days - like above - would have the obvious advantage of being the same across Europe, not being subject to any doubt, difference, bias or local judgment, thus securing a European “level playing field” for these kind of services. Any criterion subject to further judgment would have the risk of damaging the level playing field, or to maintain artificial unequal situations across Europe. This should be best avoided whenever possible.

In accordance with the sound experience in the UK, a period of 7 days is a good choice. We are of the opinion that any shorter period would be disadvantageous for the liquidity of the market, prohibiting in particular smaller market participants from entering and participating in the market.

Therefore, responding to question number 2.7.:

- ***We do agree that there should be an initial filter for spot markets.***
- ***We do not agree with the criterion of “the lesser of two business days and the generally accepted settlement period in the relevant market”, for reasons as set out above.***
- ***We prefer the criterion of a fixed number of working days, preferably seven as currently in the United Kingdom.***

We would ask you to consider that the latter choice would be positive for the liquidity in short-term energy markets (gas and electricity) across Europe.

This would providing a better determination of gas and electricity prices for the end consumer, as well as a robust daily market price providing a reference for long-term contracts being necessary for the security of supply.

Some more detailed comments and responses to some of the questions in the document are contained in the attachment.

Sincerely yours,

Bert den Ouden
APX group

ATTACHMENT

Detailed comments and responses to questions

Subject: *comment on consultation document*, CESR's draft technical advice on the implementation of directive 2004/39/EZ on markets in financial instruments; in particular regarding energy commodities electricity and gas.

Question 2.1

"commodities" not to be limited to "goods", should include rights and property that are (primarily) traded for commercial purposes i.e. not investment purposes.

Question 2.2

See 2.1 above: yes

Question 2.3

Yes

Question 2.4

Within scope of paragraph C(10) of Annex 1; although bandwidth could be traded for investment purposes, its use requires complex infrastructure and measuring. This makes it more likely that bandwidth rights would normally be traded for commercial purposes i.e. its actual use.

Question 2.5

It is not desired to have commodities restricted to goods. However, if such were the case, a requirement that there must be a liquid market in the underlying would cause difficulties in respect of the definition of "liquid". This is in particular the case since (1) liquidity in markets for goods tend to fluctuate considerably from time to time subject to surrounding circumstances affecting the ability to i.e. grow, harvest or deliver and (2) the measure of liquidity i.e. whether a market is liquid or not highly depends on the commodity itself, as well as the characteristics of players in the market.

Question 2.6

Capable of being delivered: yes

Capable of being traded: yes

Requirement for liquid market: no, see 2.5

Question 2.7

Do not agree with the proposed approach of excluding contracts whose settlement period does not exceed the lesser of two business days and the generally accepted settlement period in the relevant market. In particular in respect of electricity - and to a lesser extent gas as well - the ability to make or take delivery at commercially acceptable prices may vary from time to time. Circumstances or perceptions thereof tend to affect liquidity in these markets significantly. Parties trading electricity/gas for commercial purposes need to be balanced at the time of delivery. In order to enable balancing - and prevent undesirable

effects in terms of economy and society - parties need be able to start balancing in advance of delivery. Common market practice at the time (electricity) is to start balancing 1 to 2 weeks in advance of delivery.

Limiting spot to a settlement period of two business days, also affects the accessibility of that market for smaller players, that tend to drive liquidity and thus the ability to balance. See further comment in the main letter from APX.

Question 2.8

Considering the extend of vertical integration one tends to see in commodity markets, status of parties may (1) vary from time to time and (2) virtually impossible to measure.

Question 2.9

A commercial merchant can be differentiated from a speculator through its ability to make or take delivery (or not).

Question 2.10

Yes.

Question 2.11

Conclusive.

APX B.V.