

Opinion of the BaFin-Group¹
within the scope of the committee procedure pursuant to Article 64 Section 2 in connection with Article 4 Section 2 of Directive 2004/39/EC on Markets in Financial Instruments

I. The definition of the term „commodity“

According to the European Court's of Justice understanding, commodities are physical objects of market value and may be subject-matter of commercial transactions.² On the basis of this argumentation and the notion that the scope of application of financial supervision should not be extended disproportionately, only those commodities for which there is a commercial market – which might develop a market price for this product - should be also considered as base values for financial instruments. This is based on the assumption that standardizes products may be traded in large volumes with a certain trade frequency and that this market knows different providers. As a matter of principle this applies only to national markets. Thus, a **definition** of the term “commodity” could be as follows:

„Commodities within the meaning of this Directive are assets having a trading value and are eligible to be object of transactions meaning that they are as a matter of principle, constructed in such a way that due to their liquidity a market price may develop with regard to the product. An indication of this is the fact that they may be traded on a national market.“

In application of this definition products such as warmth, cold or states of aggregation such as e.g. steam are not considered as commodities within the meaning of the FIMD. There is no established and open trade market for the aforementioned products. They are constructed in such way that they cannot be traded. They are regularly provided at local level by sole providers. Therefore a market price cannot be established. No commodities are the indices mentioned in Annex I section C no. 10 of FIMD.

II. Circumstances under which derivative contracts relating to commodities which can be physically settled, are considered as being concluded for commercial purposes (2)

1. Explanatory Remark

Annex I section C no. 7 of the FIMD reads:

“(7) Options, futures, swaps, forwards and any other derivative contracts relating to commodities, that can be physically settled not otherwise mentioned in C.6 and not being for commercial purposes, which have the characteristics of other derivative financial instruments, having regard to whether, inter alia, they are cleared and settled through recognized clearing houses or are subject to regular margin calls;”

In consideration of the legislative procedure which lead to the adoption of the FIMD we assume that the term “not being for commercial purposes” has not been introduced into the Annex I section C no. 7 intentionally but due to an occasional error. This assumption is made

¹ The BaFin-group is a group of about 20 national and international enterprises of the energy market. Since the middle of the year 2001 the BaFin-group has been dealing with the adequate application of the German banking law to the energy market.

² European Court of Justice (EuGH) Rs. C-393/92, Slg. 1994 I 1477 Rdnr. 228 = DVBl 1994, 852.

against the following background: The FIMD has been adopted in the co-decision procedure pursuant to Article 251 EU Treaty. This means that European Parliament has a right to introduce own amendments into a draft directive. Accordingly, the European Parliament adopted in its Second Reading on March 30, 2004 amendments inter alia to the list of financial instruments in Annex I section C of the FIMD. One amendment was Annex I section C no. 6a. It extended the list of financial instruments coming under the directive's scope of application. Annex I section C no. 6a contained the wording: "...having regard to whether, inter alia, being traded for commercial purposes...". One can find the wording "being for commercial purposes" also in number 8b of Annex I section C another extension to the list of financial instruments introduced by the European Parliament in its Second Reading.

The European Council adopted the European Parliament's proposal for the FIMD on April 7, 2004. Since the FIMD had to be adopted in the co-decision procedure pursuant to Article 251 EU Treaty the European Council had to adopt the FIMD including all amendments introduced by the European Parliament. Thus, the provisions of the adopted version of the FIMD have to correspond with the version adopted by the European Parliament in its Second Reading. And accordingly we assume that the term in Annex I section C no. 7 of the FIMD "and not being for commercial purposes" has to be read as "and being for commercial purposes".

The BaFin-group wishes to emphasize that this assumption is made on the basis of the documents available at the homepage of the EU. Notwithstanding this assumption, the BaFin-group is aware that other EU documents of before the date of the second reading of the FIMD are at hand which imply that the final version of the FIMD is correct. If the understanding of the documents currently available at the homepage of the misled the BaFin-group's conclusion, the BaFin-group wishes to withdraw the assumption of above. In this case the BaFin-group proposes to interpret the term "non commercial purposes" as follows: The absence of a speculative interest as defined under III 2 b below should create the assumption that an enterprise does act with a non commercial purpose.

2. Definition of the characteristic „for commercial purposes“

The term "for commercial purposes" relates to the derivative transactions listed in Section C.7³.

Firstly, we propose an interpretation which corresponds to an interpretation of the term as "*commercial / on a commercial basis*". An activity on "*a commercial basis*" is generally regarded as an activity which is designed to have certain duration and with the *intention to draw profits*. Business transactions of an enterprise conducted once or twice are not designed to have certain duration.

Moreover and primarily, the classification for "commercial purposes" respectively as "acting on a commercial basis" requires a corresponding motivation relating to the business. The enterprise's market appearance must be constituted in such a way that the provision of (financial) services takes priority in the enterprise's business activities. An enterprise e.g., which delivers electricity to third parties and at this opportunity sells or buys a small number of derivative contracts relating to the base value electricity from its portfolios, in order to ensure an optimal portfolio management, does not act on a commercial basis with regard to these derivatives and therefore not for commercial purposes. The enterprise's primary motivation to act is the delivery with electricity. Consequently, the differentiation of the characteristic "for commercial purposes" depends on the composition of the portfolio of the enterprise dealing with base values of derivative financial instruments.

In contrast to this, business transactions "for commercial purposes" in connection with financial instruments are regular business transactions with the intention to draw profits, which do

³ Articles, references to annexes and enumerations refer to – unless otherwise provided – Directive 2004/39/EC.

not exceed a certain volume and cannot be classified as an ancillary service of the transaction in commodities.

Circumstances suggesting that the transactions in question do not serve commercial purposes, may be in particular:

- The rare occurrence of such transactions;
- The classification of such transactions as of subordinate importance (ancillary services) with regard to the main business;
- The small absolute amount of the total portfolio which includes derivative products;
- The narrow market with regard to the transactions in question in comparison with non-derivative transactions irrespective of the amount of the portfolio;
- The trading enterprise's inexperience in the trade, to which the transactions in question belong;
- The enterprise's missing intention to draw profits from the transactions in question, which can be concluded from the enterprise's business plans or other objective clues.

2. No separate examination of the characteristic "for commercial purposes"

In response to the question raised in the „Call for Evidence“, whether the characteristic "for commercial purposes" shall be treated cumulatively or separately, it is suggested to consider the characteristic as independent criterion and to examine it combined with criterion "otherwise have the characteristics of financial instruments" (for characteristics of other derivative financial instruments see 4.) and not keep it separately. The consequence of a separate examination, which certainly does not correspond to the aim of the directive, could be that transactions in commodities – which although being for commercial purposes, do not have any characteristics of other derivative financial instruments (as listed under 4.) – are regarded as financial instruments within the meaning of the FIMD.

III. Definition of the characteristics „other derivative financial instruments“ for derivative contracts within the meaning of Section C.7 (3)

1. Clearly defined criteria

„The characteristics of other derivative financial forward transactions“, which are to be developed with regard to the definition of financial instruments (Annex I Section C.7), shall be preferably unambiguous and clear-cut and ascertainable on the basis of objective circumstances. At the suggestion and in cooperation with the BaFin-group the German supervisory authority for financial services (BaFin) developed criteria which define a "derivative financial forward transaction". These criteria having been tested in practice give consideration to all interests, because their application prevents the classification of every forward transaction relating to an exchange of commodities as derivative financial forward transaction and the coming under supervision of the parties involved. The license requirement involves a couple of consequences (e.g. higher capital adequacy requirements and obligations with regard to company organization), which lead to considerable difficulties for commodity traders. In respect of selecting criteria it has to be taken into account that real exchange transactions do not come under the application of the FIMD on the basis of a too broad interpretation of the criterion "derivative financial forward transaction" – particularly against the background that especially transactions relating to electricity must always be concluded "forward" since the commodity electricity cannot be stored. In detail:

2. Elements of Differentiation

According to Annex I Section C.7 derivative contracts which can be physically settled and are not traded on a Regulated Market/ MTF come under supervision.

This shall be the case (according to the justification on the Directive) when they have characteristics of other derivative financial instruments. Therefore, the starting point for the considerations lies in the term "derivative".

a. Derivatives and Intention of Interpretation

Derivatives are outright forward transactions or option contracts whose price depends directly or indirectly on the stock exchange or market price of a reference value (here: commodities). An outright forward transaction is a transaction pending between conclusion and maturity, and which has not been settled by both parties. One characteristic of buying forward e.g. is the fact that the object of purchase is to be delivered and paid at a deferred point of time. An option contract in its typical form is a contract which entitles a party, the buyer of options, against premium payment to conclude a transaction on the basis of predetermined conditions by issuing a unilateral declaration of intent at or up to a specific future date. Until exercising the option right the buyer of options is only entitled, but not obliged to conclude such a transaction.

The definition of derivatives as outright forward or option transactions includes the concept of forward transactions. So far European and national legislators, jurisdiction and literature have not succeeded in developing an adequate definition which considers all manifestations of forward transactions. Assuming, however, that a forward transaction is merely characterized by the fact that the time of delivery differs from the conclusion of the contract, for commodity traders dealing with storable commodities such as e.g. electricity this would lead to the unintentional consequence that the conduction of trade transactions would require a banking license. A nearly complete supervision of electricity supplying companies, including their classical business of supplying e.g. end-consumers with electricity without ever needing a banking license for decades, would thus be the consequence. This interpretation does certainly not correspond with the FIMD.

The impossibility of defining the term „forward transaction“ with regard to all kinds of cases, suggests to regard this term as a type which is determined by a number of characteristics, where the existence of all characteristics is not always mandatory, but which determine the appearance of the transaction as a whole. According to the view of the German Supervisory Authority BaFin such typical features include:

- The possibility to participate disproportionately in price changes with a relatively low initial investment (**leverage effect**);
- The **risk of total loss** of initial investment that exceeds the regular insolvency risk;
- The **risk** of having to provide **additional funds** to cover liabilities, against what has been originally intended.

This typology, which is primarily based on three elements, has been further refined in view of the government justification with regard to the 6th amending law of the German Banking Act and the spirit and purpose, explained therein, of supervising services in connection with commodity forward transaction by the BaFin. A survey of the year 1995, conducted with the Confederate and Federal law enforcement authorities by the Federal Ministry of Finance, showed that since 1990 ten of thousands of investors suffered losses with regard to the distribution of financial futures, forward exchange transactions and penny stocks as well as, in particular, the distribution of commodity futures. This would justify a special supervision for reasons of investors' protection. If, however, the idea of protecting investors is the central reason for supervising services in connection with commodity futures, also the typology of transactions must take into consideration the point of view of potential investors as well as the risks of possible financial investments. In view of the Financial Supervisory Authority's

safeguard function it seems to be justified that only those transactions are typologically regarded as forward transactions within the meaning of the standard,

- which are deemed an offer of financial investment by a **potential investor**, i.e. a possibility to draw profits speculatively.

In contrast to this, energy markets have their own special situation: Due to the fact that on the one hand electricity cannot be stored and gas is only storable to a certain extent and the necessity of security of supply on the other hand, there is with regard to electricity supply contracts a higher economic demand of forward transactions, i.e. supply contracts with a deferred maturity date. Even if electricity or gas trading enterprises conclude forward supply contracts with the intention to sell the purchased commodity at a profit, (according to BaFin's view) the subject-matter is comparable with the subject-matter of ordinary cash transactions with regard to the delivery of goods: a "real" profit (arbitrage) shall be drawn. The conclusion of forward transactions is considerably based on the fact that electricity and gas cannot or only to a limited extent be stored. The very fact that a trader would assume an obligation to deliver empty thereby exposing himself to the risk of higher replacement costs, could not justify the assumption of a commodity derivative, even if one or more of the mentioned typological criteria might apply. Therefore the following applies:

If trading transactions stipulate a **physical settlement** and thus the buyer's obligation to accept, these transactions are not regarded as financial investment possibility by a potential capital provider. In fact, such transactions are considered as cash transactions by the buyer. The buyer must assume (and also wants to do so) that in case of doubt he has to provide the capital necessary for the settlement of the purchase price or to collect the previously agreed amount of electricity. Therefore such delivery transactions concluded e.g. by municipal utilities to satisfy their end-users' needs do not require a license (since derivatives are not involved). A delivery action with deferred settlement, however, is regarded a derivative forward transaction, if the transaction is obviously aimed at not being physically settled. In cases where a buyer's obligation to accept may be reduced to a cash settlement, it can be assumed that from a potential investor's point of view such a transaction is regarded an investment or speculative transaction and also used as such. Here a leverage effect seems possible, which provides the opportunity to disproportionately profit from possible price fluctuations ("difference intention") by the notional closing of the transaction with a relatively low initial investment and to realize the risks related therewith for the investor. If, in contrast to this, there is no intention to profit from price differences ("no difference intention"), because as pointed out especially physical settlement is intended, it is an ordinary deferred transaction.

The BaFin always assumes an enterprise's "difference intention", if the respective contractual party is not able to collect or deliver electricity at the agreed amount or collection is unusual with regard to the other party's professional or commercial business. A stereotypical organization of a transaction may be an indication for a "difference intention". On the other hand the existence of balance areas and scheduled declaration of a concrete delivery or also the status of the enterprise as general supplier may be an indication for a "physically motivated" interest in the organization.

b. Relevant characteristics

Not all criteria of differentiation as mentioned under (a) – (e) are necessarily mandatory with regard to a transaction. It is important that the overall assessment is in favour of a financial instrument or against a forward commodity exchange transaction.

- (a) Possibility to participate disproportionately in price changes with a relatively low initial investment (**leverage effect**);
- (b) **Risk of total loss** of initial investment, which exceeds the regular insolvency risk;
- (c) **Risk of having to provide additional funds** to cover liabilities, against what has been originally intended;

- (d) **Physical settlement** of the transaction is legally and/or de facto not possible;
- (e) **Speculative interest of the acting party** (= no interest in acquiring the base value).

The BaFin-group suggests to include the typifying characteristics with regard to the concretization of Section C.7 of the FIMD. For the characteristics in detail:

- **Leverage effect**

The so called leverage effect is based on the fact that price fluctuations have a considerably stronger impact on the rate of derivative financial futures than on the rate of the underlying base value.

- **Risk of total loss of initial investment**

In correspondence to the leverage effect, there is the risk that one contractual party – if prices develop against what has been anticipated – is not given value for its performance and thus loses its initial investment completely.

- **Risk of having to provide additional funds**

With regard to derivative financial futures there is also the risk of having to provide additional funds in order to cover future liabilities, if market or stock exchange prices develop against what a party has expected.

- **Financial Settlement**

A typical characteristic of a derivative financial future is the possibility of financial settlement. This means that according to the regulations of the forward transaction there is – either exclusively or at least at the option of one contractual party - only a financial settlement of contractual liabilities. In particular with regard to those commodity forward transactions, where beside a financial settlement there is also the possibility of physical settlement, a differentiation between a commodity exchange transaction with a deferred settlement date and a derivative future transaction proves to be difficult to some extent. Here the decisive condition is that the aforementioned characteristics (a) – (c) and in particular the speculative interest as described under (e) apply to be able to speak of a financial future.

- **Speculative Interest**

Finally, one basic criterion of derivative financial futures is the parties' speculative interest. If one of the transactions listed in number 7 was subjectively concluded with a speculative interest, it can be concluded from the fact that the parties to the transaction objectively do not have any interest in an actual exchange of the base value. A speculative intention e.g. can be assumed if the respective contractual party is not able to collect or provide the base value physically, e.g. if it has not obtained official licenses or the transaction is unusual for the general activities of the contractual party. In contrast to this, the fact that the contractual parties have the legal and effective conditions to settle the transaction physically and transactions above the base value of the contract correspond to subject-matter of their business speaks against the conclusion of a transaction from speculative motives and thus, speaks for an interest in the physical settlement of the transaction. According to the BaFin-group's view transactions are at any rate not regarded as speculative when the total trade volume of the base value does not exceed 200 % of the actual purchase quantity of a contractual party.

c. Classification

If the differentiation criteria under b (a) – (e), which were developed by the BaFin-group, are applied to commodity forward transactions on commodity markets, the following classification applies:

Therefore no derivative financial futures are:

- Physically settled electricity and natural gas supply contracts as well as physically settled crude oil and coal supply contracts with end-users: These transactions are

de facto physically settled. There is no speculative intention. Consequently, these transactions are – regardless of their deferred settlement date – no financial futures within the meaning of the FIMD.

- Also physically settled electricity and natural gas supply contracts, which partly include energy prices indexed as “embedded derivatives”, are no financial futures. The indexing does not justify the contracts’ characteristic as derivatives within the meaning of the FIMD, since there is no difference between the originally agreed price and a later value of the transaction, which could be used for speculative purposes.
- Physical OTC-spot electricity and natural gas trading transactions under the EFET General Agreement. These agreements are physically settled and provide no opportunity for speculation.
- Physical forward electricity and natural gas trading transactions under the EFET General Agreement, natural gas trade at the Zeebrügge Hub under the ZBT terms and conditions 2001 as well as natural gas trade at the National Balancing Point in the UK under the Short Term Flat NBP Trading Terms and Conditions General Agreement 1997 or physical forward electricity trading transactions under GTMA in the UK: These transactions are physically settled and do not have the typifying characteristics which are relevant for the differentiation of commodity derivatives (forward transactions) and mere delivery transactions with a deferred settlement.
- Transactions with exchange traded spot products: Exchange traded spot products are traded as hourly contracts, block contracts of the hourly auction, baseload contracts, peakload contracts and weekend baseload contracts. These spot market transactions are aimed at physical settlement. The physical delivery takes place on the next delivery day after the trading day and on all weekends and public holidays directly succeeding the trading day and the delivery days succeeding these weekends and public holidays. These transactions are characterized by a timely settlement date after the conclusion of the transaction. This timely settlement date offers no opportunity for speculation with regard to the conclusion of these transactions, because the electricity price does not considerably change within these time limits of max. six to seven days.

Therefore derivative financial instruments are:

All contracts to be exclusively financially settled which may be used for speculative purposes such as e.g. financial forwards, futures, floors, caps, financial options, collars.

IV. Definition of climatic variables, freight rates and emissions allowances (4)

For the definition of the basic values contained in Section C.10 we propose the following typological criteria.

- **Climatic variables**

Climatic variables are all variables which refer to measures based on climatic circumstances or processes. Such measures can in particular arise out of temperature, precipitation, air pressure, insolation and wind.

- **Freight rates**

Derivative contracts based on freight rates are those contracts which are related to the average transport costs of commodities. Transport costs are costs for a certain type of freight on a certain transport route and under certain transport conditions. Transport conditions are inter alia transport time, means of transport and capacity of transport. Freight

rates are considered to be a financial instrument only if they really serve as underlying for a transaction. In this context it can be referred in particular to the freight rates which are traded on exchanges (e.g. on the Baltic Exchange in London). A contract which is purely an agreement with respect to the transport of commodities if the effective transport is the main subject of the contract is no financial instrument.

- **Emission allowances**

Emission allowances in the meaning of the FIMD shall be officially granted allowances which entitle an entity to emit within a certain period a certain amount of emissions harmful to the environment. In context with the emission trading in the European Union these criteria should be restricted in two ways:

Emission allowances which have been purchased for the compliance with the divestiture obligation pursuant to article 12 para. 3 of the Directive of the European Parliament and Council of October 13, 2003 regarding the system for the trade with greenhouse gas emission certificates in the European Union and the amendment of the directive 96/61/EC of the Council (Emissions Trade Directive) should not be considered as emission allowances in the meaning of the FIMD. Pursuant to article 12 para. 3 of the Emission Trade Directive the Member States are obliged to make sure that undertakings which are subject to the emission trade submit until the 30 April of each year a number of certificates which corresponds with their emission in the previous year. The therefore purchased allowances are solely meant for the compliance with the emissions reduction obligation. They are only a means of evidence and are not traded with the intention to gain a speculative profit. Thus, it arises no danger neither for the financial markets nor for the perspective of the investors' protection which would require supervision. Such an interpretation would correspond with the differentiation between derivatives and non-derivatives in the electricity trading sector as opined by the BaFin for its area of supervision.

Accordingly, the following has to be reckoned: These transactions do not have the typifying characteristic „speculative intention“, which differentiates derivative financial instruments from mere delivery transactions with deferred settlement. The trade in emission allowances is settled physically. According to Section 16 of the German Greenhouse Gas Emission Allowance Trading Act (TEHG) emission allowances are transferred through mutual consent and record of the transfer on the purchaser's account. To settle a transfer claim it is not necessary to physically deliver the allowance, but it is sufficient (besides the mutual consent) to record the emission allowances on the purchaser's account, which is kept in the emission register (Section 14 TEHG). Thus, this legal transaction is not only financially settled transaction, but also includes, beside the payment of the price, the transfer of property in allowances. This also shows the ISDA Master Agreement on the Transfer of Emission Allowances. Under number 2 on page 3 of the Master Agreement it reads “settlement method”, “physical settlement”. Therefore transactions with regard to the transfer of emission allowances are to be settled de facto. This is only consequent, since emission allowances are transferred on the condition that allowances are registered for the purchaser.

Secondly, emission allowances should not be regarded as emission allowances in the meaning of the FIMD if they are transferred from the register of the seller to the register of the purchaser and this transfer lasts more than two days. In this case the transfer would not be considered anymore as a spot transaction which would lead to a categorisation as a forward rate agreement in the meaning of the FIMD. But in this situation no one of the participating parties of the transaction can control or influence the precise time of the transfer of the certificate and fulfilment of the contract. Hence, it would not be justifiable to consider such contracts as derivative transactions. The exclusion of the emission

allowances which are reserved to transfer or/and are in handling would lead to adequate consideration of this factor.

V. Differentiation between investment consulting article 4 para. 1 no. 4 and general information

A criterion for the differentiation of the “personal recommendation” on the one hand and “general recommendation”, “marketing communication” and “simple offers” on the other hand is the concrete and individual information adjusted to a client in distinction to the general information which approaches a potential abstract number of clients. In this respect it is decisive whether the information is for remuneration meaning that the informing person awaits for its information a valuable consideration. Information for remuneration indicates investment consulting (also arg. Article 2 para. 1 lit. (j) FIMD); the information inspires a particular value of the consultation and intensive occupation with the information's background. A factor which speaks against the existence of investment consulting is the delivery of statements of a certain generality without knowledge of the personal situation of the client and the special situation.

A further criterion for the differentiation is the question whether the information has been delivered on basis of a particular expertise of the informing person, his experience and under the availment of a particular clients' trust based or whether the information has been given solely for informational reasons. The latter speaks for a general informational statement. In context with the differentiation between a “personal recommendation” and a simple information of a client regard will have to be made also to the fact whether the informing person connects with the information the advice for a certain action or behaviour, e.g. the conclusion of a transaction or whether the information has been given without suggesting the informed person a certain behaviour or action. A further criterion is also the existence of a consulting agreement between the consultant and the person seeking consultation.

VI. Further necessity of definition: Own account trading; market-making

The European Commission did not mandate CESR to contribute to the concretisation of article 2 para. 1 lit. (d), (e) and (k) even though the FIMD would allow the execution of the panel procedure pursuant to article 64 para. 2 in context with article 2 para. 3 too. The same applies to the definition of the terms in article 4 para. 1 in particular no. 6 (own account trading) and no. 8 (market-making). Article 4 para. 2 would have allowed a consultation mandate for CESR in this case as well. A participation in the concretisation of the exemption provisions of article 2 para. 1 lit. (d), (i) and (k) and connected terms in article 4 para. 1 would be important for the energy trade in order to obtain an adequate ascertainment of the FIMD's scope of application in the field of commodity trade and in order to obtain a harmonisation of the European legislation.

1. Own account trading

Annex I Section A no. 3 addresses the own-account trading as securities service. Pursuant to Article 4 para. 1 no. 6 of FIMD the own-account trading is defined as trading under the use of own capital which leads to the conclusion of transactions with one or more financial instruments.

First, it is important to ascertain that there must be a differentiation between own-account trading requiring a license and own business transactions for which no license is required. This differentiation – which is according to our opinion already indicated in the FIMD – is particularly important for commodity traders. It decides about the necessity of a license and not only about the assignment to an undertaking's trading book business as it is the case with undertakings which are subject to financial supervision anyway because they pursue banking

businesses. A license requiring own-account trading is considered to be the financial service of purchase and sale of financial instruments by way of own-account trading for others, Section 1 para. 1a, sentence 2, no. 4 KWG (German Banking Act). Thereby the institute adopts in relation to its client the role of a buyer or a seller. In contrast to the own-account trading the so called own business transactions do not require a license. Since both own-account trading and own business transactions entail an acting in their own name and on own account, the distinction between both activities lies finally solely in the intention of the activity: The own-account trader acts on basis of an order and offers its activity as a kind of service; the one who pursues own business transactions does not act on basis of an order and does not offer the activity as a form of service. Thus, the difference is the third-person relation, meaning a service characteristic. An own-account trader is clearly the one who organises upon enquiry of its client a derivative. Difficulties in the differentiation occur e.g. if the commodity is - by the time a buyer makes an enquiry - already in the portfolio or if a hedging instrument is rededicated into a trading instrument.

For the categorization as a securities service subject to license in the meaning of the FIMD several criteria are on hand:

- purchase and sale of financial instruments fall together;
- at the time of the purchase of financial instruments a relation to its sale is already existent (thus, there is an order for an activity in the interest of a client's purchase or sale order);
- there is a contract between a client and the trader having the character of a business activity conducted on instructions;
- the transaction is not solely for hedging purposes;
- the activity does not serve solely the use and the administration of own assets;
- the entrepreneur does not – from the objective point of view – use solely an existent market or a randomly available possibility for a conclusion of a contract (thus, is acting similar to a passive client);
- it is not an arbitrage activity;
- as (one) indication: the classification into either the trading or the asset book.

2. Market-maker

Persons who administrate their own assets and entities pursuing securities services and/or investment activities only in form of own account trading shall not come under the scope of the FIMD unless the are, inter alia, market-maker, Article 2 para. 1 lit. (d). Pursuant to Article 4 para. 1 of FIMD market-maker are persons which show on financial markets on continuous basis their preparedness to conduct trade for own-account on basis of rates fixed by them by way of purchase and sale of financial instruments in using own capital.

It should be made clear here at least that market-maker participating on futures markets of energy exchanges which operate as second (and marked of) market a spot market should not come under supervision. The creation of a liquid spot market is absolutely necessary in the just arising energy trading market and is operated on just one exchange in the respective country.

3. Ancillary business and main business

Article 2 para. 1 lit. (i) stipulates that FIMD does not apply to

- Persons dealing on own account in financial instruments, or providing investment services in commodity derivatives or derivative contracts included in Annex I, Section C.10 to the clients of their main business, provided this is an ancillary activity to their main business, when considered on a group bases, and that main business is not the provision of investment services within the meaning of this Directive or banking services under Directive 2000/12/EC;

Article 2 para. 1 lit. (k) stipulates that the FIMD does not apply to

- Persons whose main business consists of dealing on own account in commodities and/or commodity derivatives. This exception shall not apply where the persons that deal on own account in commodities and/or commodity derivatives are part of a group the main business of which is the provision of other investment services within the meaning of the Directive or banking services under Directive 2000/12 /EC.

A clarification when a main business will develop into an ancillary business or converse would be desirable. It has to be clarified in particular in this context further what has to be considered as "pursuant of own account trading with commodities and/or commodity derivatives" in order to ascertain this scope of the directive.

Dr. Ines Zenke
Rechtsanwältin

Dr. Ralf Wagner
ConEnergy AG/Essen

Becker Büttner Held
Rechtsanwälte Steuerberater Wirtschaftsprüfer
Becker Büttner Held
Köpenicker Straße 9
10997 Berlin