

Committee of European Securities Regulators
Mr. Fabrice Demarigny
Secretary General
11-13 Avenue de Friedland
F-75008 Paris

21 January 2005

EURELECTRIC response to the Consultation on CESR's draft advice on the second set of mandates from the European Commission on the Markets in Financial Instruments Directive (MiFID), Ref. CESR/04-562

Dear Mr. Demarigny,

EURELECTRIC is happy to comment within the level-2 process concerning possible implementing measures of the Directive on Markets in Financial Instruments (MiFID). EURELECTRIC represents the vast majority of European electricity producers and suppliers. We welcome the extensive reflection that CESR has made with regard to the second mandate.

As already stressed before (see our letter of 29 July 2004), EURELECTRIC welcomes the overall intention of the European institutions not to subject the average energy firms to financial regulation. However, as some energy companies will in any case become MiFID-regulated, it is important that sufficient clarity is achieved in implementing the provisions of the Directive on national level, especially as far as it concerns the particular issue of commodities and commodity derivatives trading.

We would also like to point out from the beginning that energy firms are subject to specific sector regulation governed by Directives 2003/54/EC for electricity and 2003/55/EC for gas. These Directives are currently in the course of being transposed into national laws and will significantly contribute to a Europe-wide energy market. As these Directives will provide the legal framework for the internal energy market, it is necessary to make sure that financial regulation, especially MiFID, supports liberalisation and does not have an adverse impact on the energy market liquidity. Liquidity of the wholesale markets and a proportionate approach to regulation are key issues for the electricity industry. The emergence of power exchanges and the development of the power futures and forward market offer not only a new business segment, but also products and mechanisms to manage the risks that coincide with competitive markets, such as price and volume risks. Careful consideration of regulatory aspects is therefore required, in order to foster and consolidate these markets.

As noted above, we have already sent you a letter dated 29 July 2004, as a response to the CESR call for evidence. The points presented in the letter are still valid. To emphasise some of those aspects, we would like to briefly highlight the following points.

Investment advice

We do not believe that the bilateral communication between the investment firm and the client or potential client is sufficient to determine whether investment advice according to the Directive exists. It is important to differentiate personal recommendations from general recommendations and marketing communications. The main criteria is the fact that a personal recommendation is subject to a valuable customised recommendation/advice. The purpose of such a recommendation is to provide the customer with an individual recommendation/advice regarding transactions relating to financial instruments. We believe that it is appropriate to restrict "investment advice" to recommendations of specific financial instruments listed under Annex I Section C and should not cover generic information such as financial planning and asset allocation services for financial instruments.

3.1.1 Definition of Commodity

We believe that the term commodity should be limited to goods. As generally accepted today, electricity is a commodity, and should therefore be included in the definition.

As the CESR draft advice also suggests, EURELECTRIC does not think that energy transport capacity, such as electrical network transmission capacity, should be considered a commodity.

3.1.2. Commercial purpose

Spot transactions

It is vital that all spot transactions remain outside the scope of MiFID and are therefore not considered under Annex I.

EURELECTRIC does not agree with the CESR draft advice to use a test which takes the lesser of two business days and the period generally accepted in the relevant market as the standard delivery period to define whether a contract is a spot contract. A 2-day test would not cover all commodity markets, some of which have considerably longer delivery periods. As electricity is not storable, a two business day rule is in a lot of cases not feasible. The period generally accepted as the standard delivery period in electricity markets can in fact be over four weeks in some cases.

EURELECTRIC therefore proposes to amend the wording "*delivery is to be made within the lesser of*" in Paragraph (1)(a) of Box 3. The suggestion would be either to reformulate the phrase to "*delivery is to be made within the longer of*" or to "*delivery is to be made either (i) within 2 business days; or (ii) the period [...],*".

Furthermore, from the perspective of the energy markets, we question the logic of using a spot-market test to define 'commercial purpose'. As opposed to the underlying physical commodity, a *derivative* is a financial contract whose value is tied to the price or market value of e.g. other securities or commodities. Due to the specific characteristic of electricity, namely that it cannot be stored in large quantities and that it is grid-bound, the time of conclusion of the contracts and actual physical delivery always differ.

Generally, all these contracts whereby the commodity (electricity) is sold to customers against cash with deferred physical delivery, are normal day-to day business of power companies, and cannot be classified as derivatives. Spot transactions should therefore not be covered because they are not commodity *derivatives* (and not because a spot-market test might define whether they are for commercial purpose or not).

We also believe that exotic instruments under C10 which can be physically settled should be subject to the commercial purpose test.

Intention to deliver

We strongly support the intention to deliver test to define commercial purpose. In order to determine whether a contract should be determined not to be for a commercial purpose, it is useful to consider the intention of the parties to the contract at the time of its conclusion. As for Question 2.8., we think that the status of the parties should be considered to determine whether a contract is (or is not) for commercial purpose. It should not be limited only to determining whether exemptions in Article 2.1.(i) and (k) are applicable.

However, what concerns the intention of the parties to a contract, we would strongly like to point out that a given party can only assess his/her own intention and not the intention of the other. Therefore we do not agree with the statement in Question 2.10., by which the intention of only one of the parties would determine the intention of the contract for both parties of the same transaction.

In addition, Paragraph (3)(b) (iii) and (iv) of Box 3 should be deleted. The history of behaviour and the course of dealings between the parties is not considered as conclusive for the determination of the intention to deliver at the moment of formation of the contract being assessed.

We hope these brief comments are helpful for your work in finalising the implementation advice to the European Commission. In addition to these views, EURELECTRIC is broadly supportive of the position for this Level 2-advice put forward by some other associations, such as the German Electricity association VDEW and the International Swaps and Derivatives Association (ISDA) and the Futures and Options Association (FOA).

We remain at your disposal for any further questions.

Sincerely,

A handwritten signature in black ink, reading "Tony Cocker". The signature is written in a cursive, flowing style.

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