

VDM Energy Trading B.V.



CESR / CEBS

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Amsterdam, 24th July 2008

Response of VDM Energy Trading BV on consultation paper on CESR's/CEBS's technical advice to the European Commission on the review of commodity business

Dear Sir,

We are pleased to participate in the consultation round on commodities business. In the appendices you will find a short description of our company and the detailed answers to your questions.

In general we are concerned about the lack of liquidity we encounter in the European energy wholesale markets. To a large extent we believe this is caused by information asymmetries and lack of transparency which prevents new participants from entering the market. Also existing participants are reluctant to trade as they do not have all the relevant information.

Additional barriers in the form of capital requirements would further hamper the development of the markets. As such we believe that the additional regulatory burden should be minimized and applied as evenly as possible throughout Europe. We believe the exemption from MIFID for own account trading should be continued.

This response expresses the views of VDM Energy Trading BV on the energy wholesale markets only and does not imply or provide an opinion of Van der Moolen Holding NV.

If you have any additional questions, please do not hesitate to contact me.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'R. van der Vegt', is written over a diagonal line that extends from the 'Yours sincerely,' text towards the bottom right of the page.

Mr. R. van der Vegt
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Appendix 1 : Short company description:

VDM Energy Trading started on the 1st of January 2008. It is a 100% subsidiary of Van der Moolen Holding NV. Van der Moolen is an international securities trading and brokerage firm active in securities, futures, derivatives indexes and exchange traded funds. Van der Moolen is active on the important securities exchanges in the United States and Europe.

VDM Energy Trading is purely trading for its own account and is active in Electricity, gas, emissions and fuels in North West Europe. It is a trading member of Endex and EEX. Via a service contract we also trades in physical products and on ICE. The staff members have been active in the in the European Energy markets for over 10 years.

Appendix 2: Detailed answers

1) In practice, what proportion and/or amount of OTC commodity derivative transactions are financial instruments falling within the MIFID and what proportion are spot? (a breakdown in terms of the underlying would be helpful)

In our trading activity 100% of the trades are financial. No spot transactions are concluded.

2) Do you agree that the level of direct participation by unsophisticated investors is mainly limited to corporate clients such as producers or wholesale distributors (with a lack of experience and knowledge in derivatives markets but not in trading in physical commodity markets), that participation by private clients is very low, and that most other participants in commodity derivatives markets are sophisticated firms?

Yes, we agree with the statement

3) What informational advantages persist in commodity derivatives markets, and in particular to what extent do those also active in the underlying physical market have informational advantages?

There are a number of informational distortions in the markets:

- 1: Power plant outages (scheduled or not) are not distributed generally to the market. It requires investment in expensive third party software (e.g. Genscape) to neutralize this informational disadvantage. A system like applied at Nordpool, including punitive action, would help in rectifying the informational distortion. Such a system would have to apply at a regional level to avoid distortions between various countries (i.e. when it would be applied in The Netherlands and not in Belgium while these markets are highly related).
- 2: Gas storage levels: Access to Gas storage and actual gas storage levels and utilization rates are only published to a limited extent in The Netherlands and in Germany. Non gas storage owners are disadvantaged. A similar system like in the UK should be used.
- 3: In the Netherlands gas sales are dominated by GasTerra. The GasTerra sales formula is changed frequently and not publicly available. Only trade partners of GasTerra (mostly the incumbent distribution companies) know the formula. The formula also has impact on the TTF prices. There is thus an information distortion which favors the incumbent distribution companies. Given the dominance of GasTerra the sales formula should be publicly available.

4) Do information asymmetries in commodity derivatives markets lead to mis-selling concerns, or to other concerns about potential client detriment?

In general the lack of transparency would also give us concerns regarding mis-selling, however we are not in the client business.

5) Do you have any transparency-related concerns relating to the trading of non-electricity and gas derivatives? If so, in which markets and why?

More systematic transaction reporting and physical flows (e.g. cross border flows in Gas and power, production capacity, storage volumes) would be a great improvement with regards to transparency. In general more transparency in our view leads to better risk assessment and more liquidity. It would therefore also benefit the traditional incumbents as they are now better able to manage their positions.

6) Do you have evidence of informational asymmetries in commodity derivatives markets in relation to market abuse?

No direct evidence.

7) Please provide any information you may have on the levels of lending and trading exposures between specialist commodity derivative firms and institutions.

No information

8) What level of risk do specialist commodity derivative firms pose to the financial system?

We would expect the risk to be very limited to none.

9) To what extent does the level of systemic financial risk posed by specialist commodity derivative firms differ from that generated by banks and ISD investment firms?

Specialist commodity derivative firms are further away from the banking system and thus pose less risk to the financial system.

10) Do the risks generated by energy-only investment firms differ materially from those posed by investment firms engaging in other commodity derivative activities/services? If so, how do they differ?

We see no difference between the two.

11) Do you have any transparency-related concerns relating to the trading of non-energy commodity derivatives, and, if so, in which markets, what are the concerns, and what solutions could be applied?

None, we are only active in the energy wholesale markets.

12) Do you believe that for non-electricity and gas derivatives contracts, the transaction reporting requirements in the MIFID support market regulation? If so, can you explain why you think they do?

In general we believe that more transaction reporting provides more transparency and thus a better market. To ensure adherence market regulation seems a good option.

13) Do you have any evidence on potential problems, and if so, on the scale of these problems, that are posed by current client categorization rules?

We encounter no problems (no client business)

14) Do you have any evidence that regulation according to the main business of the group may cause competitive distortions?

No evidence

15) Do you agree that full application of CRD capital requirements to specialist commodity derivative firms is likely to impose a regulatory burden that is misaligned with their potential systemic impact?

Yes we agree.

16) Do you believe that full application of CRD large exposure requirements to specialist commodity derivative firms is likely to impose a regulatory burden that is misaligned with their business and their potential systemic impact?

Yes we agree.

17) Do you believe there is a potential for regulatory arbitrage? If so, can you provide evidence?

Yes we believe there is potential regulatory arbitrage. We would prefer a system where there would be one European regulatory regime.

18) Do you believe that the application of the MIFID organizational requirements support the intended aims of market regulation when applied to specialist commodity derivatives firms, or commodity derivatives business? If not, what aspects of the organizational requirements do you believe do not support the aims of market regulation when applied to such firms and why?

Yes we believe that it is sound practice and would help the commodities firms.

19) Do you believe that there is a case for changing the client categorization regime as it applies to commodity derivatives business? If so, do you have any evidence on the scale of the problem or potential problem posed by the existing rules?

From our point of view not relevant as we trade purely for our own account.

20) Do you believe that the conduct of business rules in the MiFID effectively support the aims of regulation with respect of commodity derivatives business? If not, can you explain why and in what respects, and whether your response is contingent upon the client categorization definitions applied to commodity derivatives business?

Yes.

21) Do each of the following elements of the criteria for determining which commodity derivatives contracts are financial instruments offer sufficient clarity to market participants to understand where the boundaries of the MiFID lie?
a) the phrase "...that must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event)";
b) the phrase "traded on a regulated market and/or MTF"
c) the definition of a spot contract in Article 38(2) of the MiFID implementing regulation;
d) the criteria in articles 38(1)(a), (b), and (c);
e) the definition of a commodity in Article 2 of the MiFID implementing regulation; and 52
f) the list of underlyings of exotic derivatives mentioned in Section C(10) of Annex I to the MiFID and Article 39 of the MiFID implementing regulation.

From our point of view there is currently enough clarity. Each of the above helps but is in itself not enough.

22) Do you have any evidence of physically-settled commodity OTC contracts being written in a way that removes them from the definition of financial instruments?

No.

23) Do you believe there are sufficient similarities between different commodity derivatives markets to make it inappropriate to differentiate the regulatory regime on the basis of the underlying being traded?

There are sufficient similarities, a preference of one regulatory regime for all energy trading activities.

24) If the capital treatment of specialist commodity derivative firms is resolved, do you think there is still a case for retaining both of the exemptions in Articles 2(1)(i) and (k)? If not, how do you think the exemptions should be modified or eliminated? If the exemptions in Articles 2(1)(i) and (k) were eliminated, what effect do you think this would have on commodity derivatives markets?

We believe there should be no capital adequacy rules for commodity derivatives firms. If these would apply and the exemptions would be eliminated then it would have a negative effect on the number of firms that participate and their volume of trading.

25) Do you believe based on the above analysis that the application of the CRD large exposures regime to specialist commodity derivatives firms is disproportionate?

Yes.

26) Do you agree that the maturity ladder approach is unsuitable for calculating capital requirements for non-storable commodities? If yes, are the proposed alternatives better suited to that task?

Yes we agree, any approach must be market based and as such a forward price curve is a good starting point.

27) Do you believe that the shortcomings identified in 2. b. and c. and 3. are relevant? Are there others that need consideration?

We agree

28) Do you think that the solutions outlined above are adequate to address these problems?

Yes

29) Do you agree with the conclusion above?

Yes

30) Which of the options presented above do you consider appropriate for the application to specialist commodity derivative firms?

A preference for Option 1; with some sort of obligation to participate in the scheme. It can not be wholly voluntarily

31) Do you think a complementary opt-in or opt-out regime could be helpful?

No, in general opt in or out leads to more uncertainty. Preferably it should be a regime that is applied throughout the EU to all participants.