

## **OPINION on position limits on ICE Argus Euro-bob Oxy FOB Rotterdam Barges contracts**

### **I. Introduction and legal basis**

1. On 20 October 2017, the European Securities and Markets Authority (ESMA) received a notification from the Financial Conduct Authority (FCA) under Article 57(5) of Directive 2014/65/EU on markets in financial instruments<sup>1</sup> ("MiFID II") regarding the exact position limits FCA intends to set for the ICE Argus Euro-bob Oxy FOB Rotterdam Barges Future and Option commodity contracts in accordance with the methodology for calculation established in Commission Delegated Regulation (EU) 2017/591 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the application of position limits in commodity derivatives<sup>2</sup> ("RTS 21") and taking into account the factors referred to in Article 57(3) of MiFID II.
2. ESMA's competence to deliver an opinion is based on Article 57(5) of MiFID II. In accordance with Article 44(1) of Regulation (EU) 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority)<sup>3</sup> ("ESMA Regulation"), the Board of Supervisors has adopted this opinion.

### **II. Contract classification**

Commodity base product: energy (NRGY)

Commodity sub product: oil (OILP)

Commodity further sub product: gasoline (GSLN)

Name of trading venue(s): INTERCONTINENTAL EXCHANGE - ICE FUTURES EUROPE

MIC: IFEU

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<sup>1</sup> Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (OJ L 173, 12.6.2014, p. 349).

<sup>2</sup> Commission Delegated Regulation (EU) 2017/591 of 1.12.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the application of position limits commodity derivatives (OJ L 87, 31.3.2017, p. 479).

<sup>3</sup> Regulation (EU) 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15. 12.2010, p. 84).



Venue product code: AEO<sup>4</sup>

### III. Market description

3. Eurobob is an unfinished gasoline primarily used in Europe. Prior to being consumed as a transport fuel, it is blended with ethanol as required by EU mandates.
4. The underlying physical market may be affected by the usual factors for commodities including geopolitical issues, weather variables and economic fluctuations.
5. For this particular contract, the underlying index provider is Argus Media, who describe in their methodology guide that their assessment is based on grades of gasoline that meet EN228 specifications with a maximum of 10ppm sulphur after they have been blended with 4.8% ethanol of minimum 98.7% purity. Oxygen content is limited to 0.9%, specific gravity is 0.755 g/ml and metal content must not exceed 1 mg/l.
6. The Argus Eurobob oxy assessment is used as a benchmark price in gasoline transactions throughout northwest Europe. The Eurobob assessment is used to price gasoline swaps and physical deals as well as by exchanges for clearing and settlement. The European swaps market shifted to price against this ethanol-ready blendstock in January 2010. The switch to Eurobob was prompted by EU mandates requiring Europe's transport fuel pool to contain a minimum of 5.75pc of biofuels by the end of 2010.
7. The Argus Eurobob price is based free on board (FOB) Rotterdam and is published daily in the Argus European Products report.
8. Trading in the Monthly ICE Argus Euro-bob Oxy FOB Rotterdam Barges Futures contracts takes place in lots. One lot is equivalent to 1,000 metric tonnes (MT). 48 consecutive months are available for trading. At expiry, the ICE Argus Euro-bob Oxy FOB Rotterdam Barges Future is cash-settled. There is no provision in the contract for physical settlement.
9. ICE also offers trading in the Argus Eurobob Oxy FOB Rotterdam Barges Average Price Options. On expiry day, options automatically exercise into the futures contract at the exercise price, i.e. at the "strike price" if the option is "in the money".
10. ICE further offers trading in ICE Argus Euro-bob Oxy FOB Rotterdam Mini, Balmo and Mini Balmo Futures. A Balmo ("balance of the month contract") is a future contract taken out on any day of the spot month and is settled on the last trading day of that month. The Balmo shares contract specifications with the whole month contract (the principal) and is price off the same underlying. A Mini contract is traded on the same trading venue as the principal contract, but in a smaller lot size. The mini and the principal contracts share all other

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<sup>4</sup> This is the primary venue product code (VPC) for this contract. However, the position limits set will apply to other associated VPCs as well. For a complete and updated list of VPCs to which the same limit applies, please check the FCA website at <https://www.fca.org.uk/markets/mifid-ii/commodity-derivatives/position-limits>.

specifications and are priced off the same underlying commodity. A Mini Balmo Future combines the characteristics of a Balmo and a Mini contract.

11. Monthly settlement is based on daily pricing in the Argus European Products Report, Euro-Bob Oxy for Northwest Europe. For final settlement, the price will be in USD and cents per metric tonne based on the average of the mean of the high and low quotations appearing in the "Argus European Products Report" under the heading "Northwest Europe" subheading "barge" for "Euro-Bob Oxy" for each business day in the determination period.
12. Argus assessment includes reference to specific standard nomination procedures where the buyer must provide 2 working days' notice of barge ETA, as regards the transactions included in the assessment. Where volume is less than 3,000 tonnes per day, the Argus assessment will default to a quotation assessment from the bid-offer range at 4.30pm London time which will be the main assessment if there is no trading and where there is some trading, the quotation assessment will form an equal part of the average with any trading volume throughout the day<sup>5</sup>.
13. ICE Futures Europe is currently the only venue trading this specific contract. A similar Argus Eurobob Oxy cash-settled contract is traded on the CME Globex platform with a 36 month maturity.
14. The estimated number of market participants is 140. There are no market makers.

#### **IV. Proposed limit and rationale**

##### *Spot month position limit*

##### Deliverable supply

15. Deliverable supply amounts to 19,130 lots. A lot is equivalent to 1,000 MT.
16. The Argus assessment reflects Eurobob in Northwest Europe so the data used to calculate deliverable supply are that of Belgium and Netherlands. Primary product receipts, import and stock data have been used in calculating deliverable supply. This reflects the Eurobob that is available in the region that could be loaded onto barges and assessed by Argus Media.
17. Deliverable supply has been calculated based on Eurostat refinery production, import and stock data for 2016 from Belgium and the Netherlands for motor gasoline oil (blended with bio components). Motor fuel is the closest proxy assessed by the FCA on the Eurostat data base as Eurobob-oxy is unfinished gasoline used as transport fuel. This data has been used due to proximity to Rotterdam as a source of the underlying product for delivery. Total imports and refinery production for 2016 were 204,470,000 MT, which divided by 12 equates

to 17,039,167 MT per delivery month. Average monthly stock levels for 2016 for the above geographical locations were 2,091,083 MT. When combined this provides a monthly deliverable supply figure of 19,130,250 MT<sup>6</sup>. This equates to 19,130 lots.

#### Spot month position limit

18. The spot month limit amounts to 4,750 lots, i.e. to 24,8% of deliverable supply. The position limit applies to the ICE Argus Euro-bob Oxy FOB Rotterdam Barges Future and Option contract and to other Balmo/Mini/Mini Balmo contracts which are based on identical core (underlying) contractual specifications, terms and conditions. The FCA's website provides an updated list showing the names and codes for these contracts.
19. The FCA is of the view that if separate limits are applied to Balmo, Mini, Mini Balmo and other types of closely related contracts the overall position of a participant on the same underlying may not be clearly represented. The FCA also considers that setting a single position limit for aggregated Balmo, Mini, Mini Balmo and principal contracts traded on the same venue where there are identical contract specifications, terms and conditions, is compliant with the objectives of the MiFID II regime and of RTS 21. It avoids the creation of multiple limits for identical commodities and the potential undermining of the overall intentions of the regime. In particular, it enhances the approach already established with the aggregation of positions under Article 57 of MiFID II and Articles 5 and 6 of the RTS 21 for same commodity derivatives and EEOCs, where positions are also aggregated with the primary on-venue contracts and become subject to one position limit. It also appears consistent with Article 3 of RTS 21, which provides for position holders to calculate their option positions on a delta adjusted basis by commodity derivative and then aggregate these with the principal commodity derivative contract.

#### Spot month position limit rationale

20. The baseline for the spot month has been set at 25% of deliverable supply as required by Article 9(1) of RTS 21.
21. The contract is cash settled against the daily Argus Euro-bob Oxy FOB Rotterdam Barges price. Therefore, factors in RTS 21 related to settlement through physical delivery are not considered relevant.
22. The method of transportation and delivery of the physical commodity including specified delivery points and capacity constraints of delivery points is not a factor for consideration as the contract does not include an option for physical delivery. Physical delivery is only relevant to the Argus assessment, which determines the price at which the commodity derivative contract is settled and is based on physical deliveries which are more than 3,000 tonnes per day in size. If there are no relevant physical deliveries, the price is set from bid/offer quotes.

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<sup>6</sup> Source : Eurostat data: Transformation output from refineries, Stock levels/closing/all stocks on national territory, Imports

23. The characteristics of the contract were considered and no adjustments were deemed necessary by the FCA. Although deliverable supply is also used as deliverable supply for other commodity derivatives, a downward adjustment has not been applied under Article 17 of RTS 21 because the contract, as well as the other commodity derivatives with the same underlying, are cash-settled. The level of deliverable supply thus does not impact on the settlement of the contract. Furthermore, the FCA has not seen evidence that deliverable supply in Euro-bob oxy is restricted or controlled or is low relative to the amount required for orderly settlement.

24. All other factors have been considered and are not regarded as material or relevant to require additional adjustments, either up or down from the baseline. In considering the volatility in the contract, as required by Article 21 of RTS 21, there has been some variation in the price of the commodity derivative but we have not found evidence that this is excessive or that lower position limits would reduce volatility.

#### *Other months' position limit*

#### Open interest

25. Open interest amounts to 16,039 lots. For the calculation of open interest, the FCA has aggregated open interest in Balmo, Mini, Mini Balmo and principal contracts traded on the same venue where there are identical contract specifications, terms and conditions and where those contracts are subject to the same position limits. The FCA considers that aggregating open interest in all these contracts provides a simpler, more consistent overview of market participant activity in accordance with the objectives of Article 57 of MiFID II and RTS 21.

26. The open interest figure has been calculated from data supplied by the trading venue. Open interest in this contract was highly variable over 2016 with peak open interest 46% greater than the average. Taking average open interest as the baseline for the position limit might prevent the market working adequately during peak periods. Therefore, open interest on the day representing the 95th percentile in terms of the level of activities has been used.

#### Other months' position limit

27. The other months' limit amounts to 4,000 lots, i.e. to 24,9% of open interest. The position limit applies to the ICE Argus Euro-bob Oxy FOB Rotterdam Barges Future and Option contracts and to other Mini/Balmo/Mini Balmo contracts which are based on identical core (underlying) contractual specifications, terms and conditions. The FCA's website provides an updated list showing the names and codes for these contracts. See also paragraph 19 above.

#### Other months' position limit rationale

28. The baseline for the other months has been set at 25% of open interest as required by Article 11(1) of RTS 21.

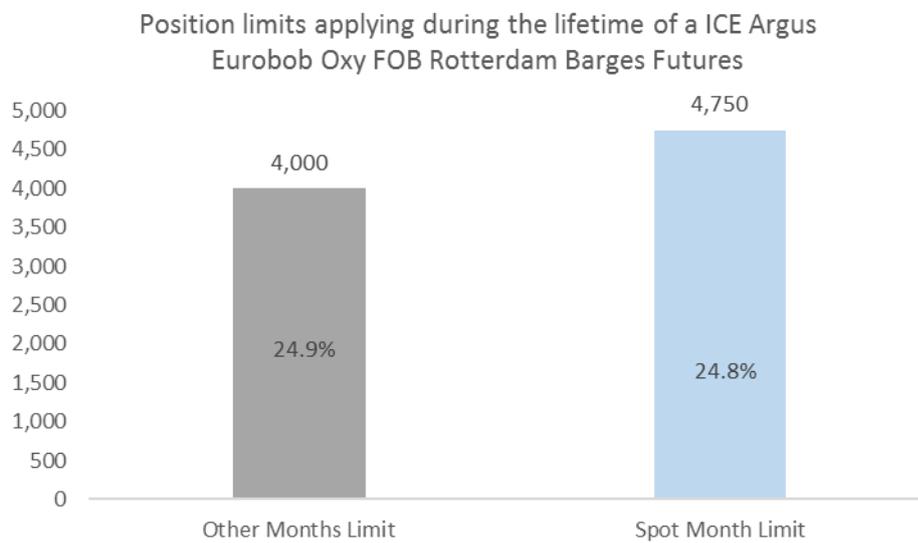
29. All potential adjustment factors have been considered and are not regarded by the FCA as material or relevant to require additional adjustments, either up or down from the baseline. In considering the volatility in the contract, as required by Article 21 of RTS 21, there has been some variation in the price of the commodity derivative but the FCA has not found evidence that this is excessive or that lower position limits would reduce volatility.
30. As no adjustments were made to the baseline of 25%, this provides a figure in lots of 4,010 lots that has been rounded down to a figure of 4,000 lots. This equates to a final limit as a percentage of open interest of 24.9%.

#### **V. ESMA's Assessment**

31. This Opinion concerns positions held in ICE Argus Euro-bob Oxy FOB Rotterdam Barges Future and Option contracts as well as in other Mini/Balmo/Mini Balmo contracts that are based on identical core (underlying) contractual specifications, terms and conditions, as shown on the FCA's website.
32. ESMA has performed the assessment based on the information provided by FCA.
33. For the purposes of this Opinion, ESMA has assessed the compatibility of the intended position limits with the objectives of Article 57(1) of MiFID II and with the methodology for calculation of position limits established in RTS 21, in accordance with Article 57(3) of MiFID II.

#### *Compatibility with the methodology for calculation of position limits established in RTS 21 in accordance with Article 57(3) of MiFID II*

34. The FCA has set one position limit for the spot month and one position limit for the other months.



\*Position limit as % of Open Interest

\*Position limit as % of Deliverable Supply

### Spot month limit

35. The calculation of deliverable supply is based on Eurostat data for refinery production, import and stock data for 2016 from Belgium and the Netherlands for motor gasoline oil (blended with bio components), divided by twelve to reach an amount of monthly deliverable supply per delivery. Considering that such motor gasoline oil is the best available proxy to assess deliverable supply for Eurobob-oxy, this approach is consistent with Article 10(2) of RTS 21, which sets out that “Competent authorities shall determine the deliverable supply [...] by reference to the average monthly amount of the underlying commodity available for delivery over the one year period immediately preceding the determination”.
36. Compared to the baseline of 25% of deliverable supply for derivative contracts where the underlying does not qualify as food intended for human consumption, the spot month limit has not been adjusted except to accommodate a rounded number of lots.
37. ESMA agrees that many of the adjustment factors set out in RTS 21 for the spot month are linked to the underlying commodity and the underlying commodity market and that those adjustment factors do not appear to be relevant for cash settled contracts such as the ICE Argus Eurobob Oxy FOB Rotterdam Barges Futures.
38. In particular, ESMA considers as a reasonable approach not to have adjusted the spot month limit downwards based on Article 17 of RTS 21 to take into account the similar Argus Eurobob Oxy cash-settled contract traded on the CME Globex platform as those two contracts with the same underlying commodity are cash settled. There is therefore no risk to orderly settlement arising from low or insufficient deliverable supply, which Article 17 of RTS 21 aims at addressing.

### Other months' limit

39. The open interest was calculated as the open interest on the day representing the 95th percentile in terms of the level of activities in the calendar year 2016. ESMA considers that such an approach is sensible in this case as it allows taking into account the seasonal peak activities in the ICE Argus Euro-bob Oxy FOB Rotterdam Barges contracts. ESMA also considers this approach consistent with Article 12 of RTS 21.
40. ESMA agrees that it is appropriate to aggregate open interest in Balmo, Mini, Mini Balmo and principal ICE Argus Eurobob Oxy FOB Rotterdam Barges contracts and to set a single position limit both for the spot month and the other months' for these aggregated contracts as they are based on identical core (underlying) contractual specifications, terms and conditions. ESMA considers that this approach is compliant with the objectives of the MiFID II position limit regime and RTS 21.
41. As for the spot month limit, ESMA also considers it reasonable not to have adjusted the other months' limit upwards or downwards as none of the potential adjustment factors under RTS 21 appears relevant. In particular, ESMA agrees that compared to other globally traded UK commodity derivative contracts, the number of market participants (140) does not appear high and consequently does not require a downward adjustment under Article 19(1) of RTS 21.

### *Compatibility with the objectives of Article 57(1) of MiFID II*

42. ESMA has found no evidence indicating that the proposed position limits are not consistent with the objectives of preventing market abuse and supporting orderly pricing and settlement conditions established in Article 57(1) MiFID II.
43. ESMA considers that these position limits have been set in accordance with the above-mentioned objectives and are suitable for the conditions under which they will be active. ESMA notes that the ICE Argus Eurobob Oxy FOB Rotterdam Barges contract is cash settled. As the settlement price of the contract is based on the average reference price published by a price-reporting agency, it is critical that the reference price is based on a sound and transparent methodology that complies with all international standards for price reporting agencies set forth by the International Organization of Securities Commissions (IOSCO) for spot market pricing.
44. Overall, the position limit set for the spot month and the other months appear to achieve a reasonable balance between the need to prevent market abuse and to ensure an orderly market and orderly settlement while ensuring that the development of commercial activities in the underlying market and the liquidity of the ICE Argus Euro-bob Oxy FOB Rotterdam Barges futures and options contracts are not hampered.



## **VI. Conclusion**

45. Based on all the considerations and analysis presented above, it is ESMA's opinion that the spot month position limit does comply with the methodology established in RTS 21 and is consistent with the objectives of Article 57 of MiFID II. The other months' position limit does comply with the methodology established in RTS 21 and is consistent with the objectives of Article 57 of MiFID II.

Done at Paris, 3 April 2018

Steven Maijoor

Chair

For the Board of Supervisors