European Securities and Markets Authority

Date: 2 September 2020
ESMA70-155-10467

OPINION on position limits on EEX TTF gas contracts

I. Introduction and legal basis

1. On 23 June 2020, the European Securities and Markets Authority ("ESMA") received a notification from the Federal Financial Supervisory Authority ("BaFin") under Article 57(5) of Directive 2014/65/EU on markets in financial instruments[1] ("MiFID II") regarding the exact position limits BaFin has set for the Dutch Title Transfer Facility ("TTF") Gas futures and options 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[2] ("RTS 21") and taking into account the factors referred to in Article 57(3) of MiFID II. The contract used to be traded on Powernext until 1 of January 2020 when the trading moved to EEX following the merger between the two entities.

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)[3] ("ESMA Regulation"), the Board of Supervisors has adopted this opinion.

II. Contract classification

Commodity base product: energy (NRGY)

Commodity sub product: natural gas (NGAS)

Commodity further sub product: TTF (TTFG)

Name of trading venue: EUROPEAN ENERGY EXCHANGE

MIC: XEEE

Venue product codes: G3B, O3B

[1] 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).
[2] 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).
[3] 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).

III. Market description

3. The TTF contract is a derivatives contract referring to the future physical delivery of gas into the Dutch transmission system. The contract used to be traded at Powernext. However, trading of derivatives contracts on gas has been moved to EEX at the end of 2019 and since 01 January 2020 all prior Powernext gas contracts are traded at EEX.

4. Natural gas is a hydrocarbon gas mixture consisting largely of methane and other hydrocarbons, occurring naturally underground (often in association with petroleum). It is used as a source of energy for heating, cooking, electricity generation, fuel for vehicles and chemical feedstock in the manufacture of plastics and other organic chemicals.

5. The Dutch wholesale market for natural gas is also known as the Title Transfer Facility (TTF). It is a virtual marketplace operated by Gasunie Transport Services (GTS). The TTF was established in 2003 to promote the trading of natural gas, thereby enhancing the liquidity of the Dutch natural gas market.

6. Derivative contracts on gas for the Dutch transmission system are the most liquid gas contracts in Europe. These contracts are not only used for hedging activities in the Netherlands but serve as benchmark contracts for other European gas markets as well. Market participants hedge their activities with TTF contracts even if their underlying businesses have no direct links to the Netherlands. This is mainly due to the fact that the Netherlands are still the most important producer of gas in Europe. A reduction of the domestic gas production has been compensated by increased imports which now make up to almost 25% of the total supply. Furthermore, the Netherlands have well-established interconnection capacities to the neighbouring grids of Belgium, Germany and the UK. As a consequence, a high number of market participants is active in TTF contracts.

7. Market participants at TTF can be classified as:

   - Utilities, which have a gas portfolio (entry/exit capacities, storages capacities, consumption clients, …) and use the market for optimizing or sourcing;

   - Industrial consumers, which are essentially buyers in the wholesale market;

   - Municipalities, which aggregate final consumers and bring their needs to the wholesale market;

   - Operators (Transport system operators, storage system operators, LNG system operators, …) which enter the system for their own needs or for balancing purposes; or

   - Trading companies which does not have a shipper or supply agreement in the market (banks, commodities traders, investment firms, …).

8. All the contracts are physically delivered via a nomination to the relevant TSO.

9. For a given trading day, EEX lists TTF derivative contracts for the next 6 months, the next 11 quarters, the next 6 seasons and the next 6 calendar years. Additionally, EEX lists options on TTF monthly contracts for the next 6 months, and bundles of 3, 5 and 12 months of the underlying, up to 34 months.

IV. Proposed limit and rationale

Spot month position limit

Deliverable supply calculation methodology

10. Deliverable supply amounts to 209,865,000 MWh.

11. The calculation of the deliverable supply is based on actual daily entry capacities of each of the entry types. While the capacities of the system are relatively stable during the year, the flows of gas depend on the consumption (not only national, but also European), which depends on the weather conditions. This calculation takes into account the following sources:

1) Entry pipeline capacity (2018) = 1,863 GWh/d[4]

2) LNG import capacity (2018) = 399 GWh/d[5]

3) Storage withdrawal capacity (2018) = 3,728 GWh/d[6][7]

4) Indigenous production (2018) = 1,005 GWh/d[8]

12. The total deliverable supply sums up to 6,995 GWh/d. Deliverable supply is expressed in MWh and calculated per standard month (30 days). Therefore, to obtain the capacity in MWh per day, the previous is multiplied by 1,000 obtaining 6,995,000 MWh per day. To obtain the monthly capacity, the capacity in MWh per day needs to be multiplied by 30.

Spot month position limit

13. Spot month limit amounts to 52,466,250 MWh, which corresponds to 25% of the deliverable supply. The limit applies to EEX TTF Gas futures and options contracts.

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4 https://www.entsog.eu/sites/default/files/2018-12/ENTSOG_GIE_SYSDEV_2017-2018_1600x1200_FULL.pdf
5 Ibidem
6 Gas Interconnection Europe: http://www.gie.eu/index.php/maps-data/gse-storage-map
7 https://www.gie.eu/index.php/gie-publications/databases/storage-database
8 Eurostat: http://appsso.eurostat.ec.europa.eu/nui/submitViewTableAction.do

Spot month position limit rationale

14. Since the EEX TTF Gas futures and options contract is not a food contract, the baseline figure for the spot month, which is based on deliverable supply, was calculated as 25% of the estimated deliverable supply, i.e. 25% * 209,860,000 MWh = 52,466,250 MWh.

15. BaFin has considered all the adjustment factors available in RTS 21 but did not deem any of those factors as appropriate to justify an adjustment either upwards or downwards from the baseline.

16. In considering the volatility in the contracts, as required by Article 21 of RTS 21, there has been some variation in the price of the commodity derivative, but BaFin has not found evidence that this is excessive or that lower position limits would reduce volatility.

17. Given the characteristics of this contract, BaFin has decided not to adjust the baseline figure. This provides a spot month limit of 52,466,250 MWh.

Other months' position limit

Open interest calculation methodology

18. The open interest amounts to 560,983,441 MWh.

19. The open interest value was calculated as the average of the daily open interest of all TTF futures from the 01 August 2019 to 31 October 2019. It was based on data provided by the European Commodity Clearing (ECC), i.e. the CCP of Powernext where the contract used to be traded before it was transferred to EEX in the course of a merger of Powernext with EEX. EEX had not listed the contract until 01 January 2020. From 31 December 2019 to 01 January 2020 all trading at Powernext ceased and started at EEX simultaneously. Accordingly, all positions held at Powernext were completely transferred to EEX. Positions in options have been delta-adjusted.

Other months' position limit

20. Other months limit amounts to 112,196,688 MWh, which corresponds to 20% of the open interest. The limit applies to EEX Dutch TTF gas futures and options contracts.

Other months' position limit rationale

21. The open interest amounts to 560,983,441 MWh. The baseline figure for the other months limit amounts to 25% of open interest, i.e. 140,245,860 MWh.

22. The following factor was considered relevant for adjusting the baseline downwards:

- Article 18(2) of RTS 21: the overall open interest is significantly higher than the deliverable supply.

23. In considering the volatility in the contracts, as required by Article 21 of RTS 21, there has been some variation in the price of the commodity derivative, but the BaFin has not found evidence that this is excessive or that lower position limits would reduce volatility.

24. All other factors have been considered and were not regarded as material or relevant to require additional adjustments, either up or down, from the baseline.

25. Given the characteristics of this contract, BaFin has decided to set a total downward adjustment of 5 percentage points resulting in an adjusted baseline of 20% of open interest. This provides another month's position limit of 112,196,688 MWh.

V. ESMA's Assessment

26. This Opinion concerns positions held in EEX TTF futures and options contracts.

27. ESMA has performed the assessment based on the information provided by BaFin.

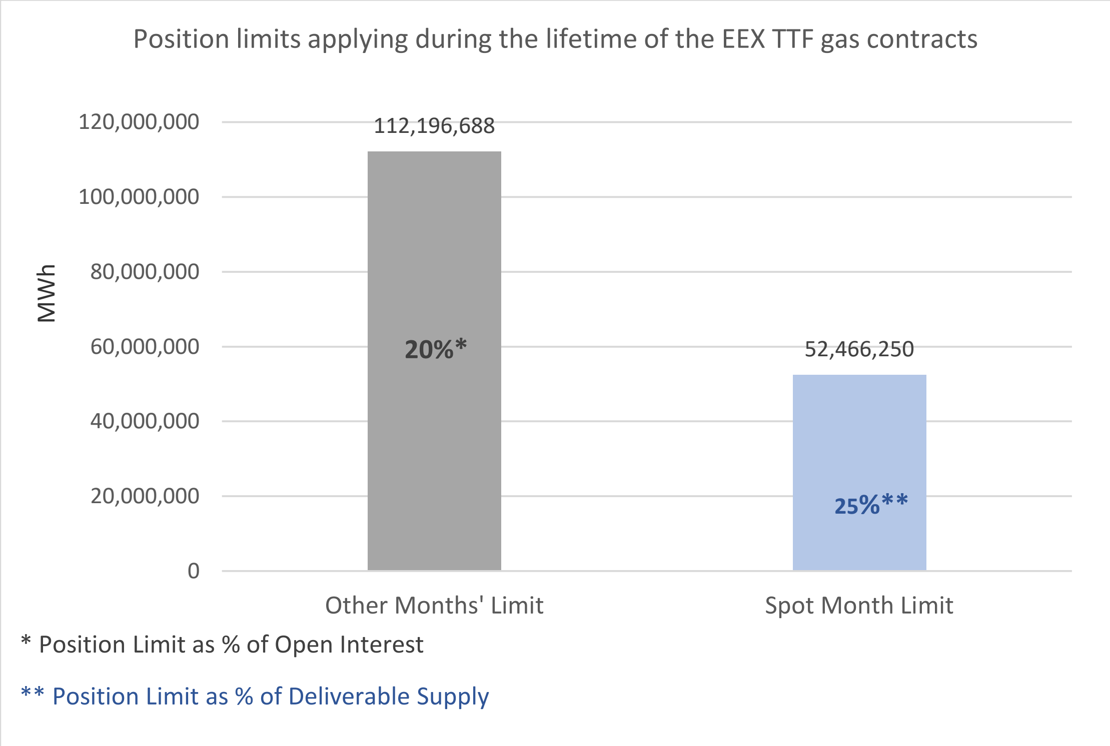
28. ESMA notes that when BaFin notified ESMA, the position limits for EEX TTF futures and options contracts had already been set and active.

29. 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.

30. Since the contract was traded before on Powernext until the end of 2019, when the merger between EEX and Powernext took place, ESMA considers that this is a continuation of trading in the previously existing contract, rather than a new contract. Therefore, it seems appropriate to use the previously observed open interest level on Powernext, for the purpose of setting the relevant position limits.

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

31. BaFin has set one position limit for the whole spot month and one for the other months.



<u>Spot month position limit</u>

32. The calculation of the deliverable supply is based on ENTSO-e figures. The estimation of deliverable supply for natural gas is calculated by aggregating Dutch gas local production, the imports and transmission capacity from neighbouring countries, LNG imports and the average withdrawal rate from storage facilities.

33. ESMA considers that the deliverable supply calculation's methodology is consistent with Article 10(2) of RTS 21 that 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".

34. ESMA agrees that given the characteristics of the contract, it is a reasonable approach not to have adjusted the baseline either upwards or downwards in setting the spot month limit.

<u>Other months' position limit</u>

35. The open interest was calculated as the daily average over three consecutive months of the number of open contracts that have not been closed out or expired. ESMA considers such an approach sensible in this case as an average for a period of time gives a more stable measure of open interest and considers such approach consistent with Article 12 of RTS 21.

36. Compared to the baseline figure of 25% of overall open interest, the other months' position limit has been adjusted downwards and set at 20% of the open interest.

37. ESMA agrees that a downward adjustment of the other months' position limit is justified under Article 18(2) of RTS 21 given that the open interest is significantly higher than the deliverable supply.

38. Consequently, these position limits have been set following the methodology established by RTS 21.

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

39. 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.

40. Overall, the position limits 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 EEX TTF Gas commodity contracts are not hampered.

VI. Conclusion

41. 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 also comply with the methodology established in RTS 21 and is consistent with the objectives of Article 57 of MiFID II.

Done at Paris, 2 September 2020

Steven Maijoor

Chair

For the Board of Supervisors