

## OPINION on position limits on EEX Spanish Power Base contracts

### I. Introduction and legal basis

1. On 2 February 2021, the European Securities and Markets Authority (ESMA) considered that sufficient information was received to assess a notification received from the Federal Financial Supervisory Authority (“BaFin”) under Article 57(5) of Directive 2014/65/EU on markets in financial instruments<sup>1</sup> (“MiFID II”). The notification is regarding the exact position limits the BaFin intends to set for the EEX Spanish Power 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<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.
3. On 29 January 2020, ESMA issued an Opinion regarding the position limits BaFin intended to set for the Spanish Power Base contracts. The position limits considered by BaFin in October 2017 were 12,814,389 MWh for the spot month limit and 14,192,000 MWh for the other months’ limit. In this opinion, ESMA concluded that the position limits considered by BaFin complied with the methodology established in RTS 21 and were consistent with the objectives of Article 57 of MiFID II.
4. According to Article 57(4) of MiFID II, a competent authority shall review position limits where there is a significant change on the market, based on its determination of deliverable supply and open interest and reset the position limit. BaFin has calculated the open interest in the EEX Spanish Power Base contracts again at the end of year 2020 based on position reporting data. BaFin considered that there had been a significant reduction in the open interest compared to its initial submission and that the position limits for both the spot month

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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, p84).



and the other months had therefore to be reconsidered. ESMA understands that the new position limits will apply upon publication of this opinion and replace the previous position limits as determined by BaFin.

5. In this opinion, ESMA is assessing whether the new position limits BaFin intends to set for the Spanish Power Base contracts comply with the methodology established in RTS 21 and are consistent with the objectives of Article 57 of MiFID II.

## **II. Contract classification**

Commodity base product: energy (NRGY)

Commodity sub product: electricity (ELEC)

Commodity further sub product: baseload (BSLD)

Name of trading venue: EUROPEAN ENERGY EXCHANGE

MIC: XEEE

Venue product codes: FEB, OEB

## **III. Market description by the competent authority**

6. The Spanish Power Base Futures contract is a cash-settled derivative contract that refers to the average power spot market price of future delivery periods of the Spanish market area. The Portuguese market area is not covered. However, Spain and Portugal form a single spot market (MIBEL) with two bidding zones. The market splits in two different prices (one for Spain and the other for Portugal) when the implicit flow of power from the results of the algorithm PCR (Price Coupling of Regions) is not compatible with the available capacity of the Spain-Portugal power interconnection. As regards the Spanish Power Base Option contracts, the corresponding futures position of the underlying asset is booked upon exercising of the option.
7. The contracts are traded in lots for which one lot equals 1MW. For futures, days, weekends, weeks, months, quarters and years are listed in parallel. For options, months, quarters and years are listed in parallel.
8. Electricity is a grid-bound commodity, where delivery takes place through meshed transmission system grids. This means that market participants have no control over the actual destination of the generated power. Electricity can only be stored to a very minimal extent, i.e. by means of battery storage. In fact, electricity is still widely considered as a nonstorable commodity. There are also some seasonal effects in the electricity market. In Spain, retail demand is seasonal, being higher in extreme weather conditions in summer and winter, and lower in autumns and specially in springs. However, such seasonal effects are small.

9. Compared to other market areas in the EU, the Spanish electricity market is - relatively isolated from the grids of its neighbouring countries due to geographical reasons and its low cross-border capacity. Its interconnection capacity remains at around 6% of overall capacity. Compared with the goal of 15% as stipulated in Regulation 2018/1999/EU this is very low.
10. Nevertheless, Spain is among those EU countries with the highest level of competition in electricity generation and an ever increasing share of renewable energy sources.

#### **IV. Proposed limit and rationale by the competent authority**

##### *Spot month position limit*

##### Deliverable supply

11. Deliverable supply amounts to 81,800,980 MWh.
12. The deliverable supply has been calculated based on statistics provided by ENTSO-E<sup>4</sup>. It is composed of the domestic Net Generating Capacity (NGC) of Spain as displayed on the Website of ENTSO-E for the year 2020 and the transmission capacities (maximum imports) from Portugal and France towards Spain from January 2020 till December 2020.
13. The Net Generating Capacity (in MW) in 2020 for Spain was 107,392 MW<sup>5</sup>. The source of data for Imports Capacity from neighbouring countries (France and Portugal) is taken from the ENTSO E - Transparency Platform and amounts up to 4,664 MW<sup>6</sup>, coming up to a total Deliverable Supply of 112,056 MW.
14. These values of ENTSO-E have been converted from yearly MW to MWh. The overall value was then divided by the factor of 12 in order to align the deliverable supply to the time frame of one calendar month for the spot month period. This results in a deliverable supply of 81,800,980 MWh.

##### Spot month position limit

15. The spot month limit is 8,208,692 MWh, which represents 10% of deliverable supply. The spot month limit applies to Spanish Power Futures and Options contracts..

##### Spot month position limit rationale

16. Since the Spanish Power Future 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.  $25\% * 81\,800\,980 \text{ MWh} = 20\,450\,245 \text{ MWh}$ .

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<sup>4</sup> European Network of Transmission System Operators for Electricity

<sup>5</sup> <https://transparency.entsoe.eu/generation/r2/installedGenerationCapacityAggregation/show>.

<sup>6</sup> <https://transparency.entsoe.eu/transmission-domain/ntcYear/show>.

17. As there are less than three market makers, the limit is to be set within a range of 5% - 50% of deliverable supply.
18. BaFin considered the following factor relevant for adjusting the limit downwards from the baseline:
  - a. the deliverable supply is significantly higher than the open interest, in accordance with Article 18 (3) of Commission Delegated Regulation (EU) 2017/591 the spot month limit is therefore to be adjusted downwards as position holders would otherwise be allowed to hold excessive amounts of overall positions.
19. All the other potential adjustment factors set out in RTS 21 have been considered by BaFin and were 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 BaFin has not found evidence that this is excessive or that lower position limits would reduce volatility.
20. Based on the above, BaFin has decided to set a total downward adjustment of 15-percentage points resulting in an adjusted baseline of 10% of deliverable supply. BaFin considered that a further reduction of the spot month limit to 5% of deliverable supply did not seem adequate as the difference between deliverable supply and open interest is not as significant as for other contracts for which BaFin set the spot month limit at 5% of deliverable supply. This provides a figure of 8,208,692 MWh.

### *Other months' position limit*

#### Open interest

21. The open interest amounts to 33,694,672 MWh. The open interest for the position limit at hand has been calculated on basis of the reports of daily net positions submitted to BaFin pursuant to Art. 58 MiFID II. The daily net positions have been added up and divided by the factor 2 ("net approach"). The number provided is the average size of daily open interest calculated on basis of daily reports from December 2019 till end of November 2020. Option positions have already been reported to BaFin delta adjusted.

#### Other months' position limit

22. The other months limit amounts to 11,793,135 MWh, which represents 35% of open interest. The other months' limit applies to Spanish Power Futures and Options contracts.

#### Other months' position limit rationale

23. The open interest amounts to 33,694,672 MWh. The baseline figure for the other months' limit amounts to 25% of open interest, i.e. 8,423,668 MWh.



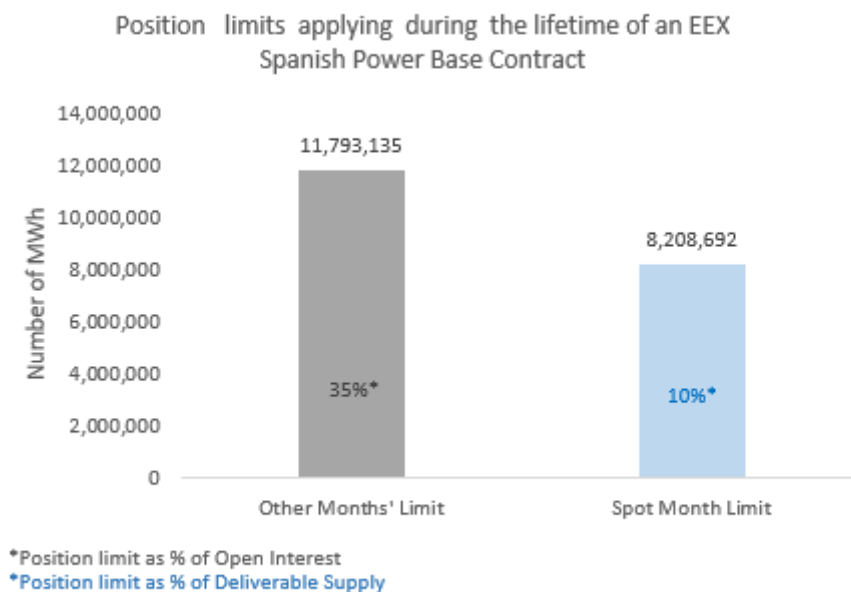
24. BaFin considered the following factors relevant for adjusting the limit upwards from the baseline:
  - a. Maturity: upward adjustment due to large number of separate expiries; in contrast to daily and weekly contracts, quarterly and yearly contracts are traded in significant volumes.
  - b. The overall open interest is significantly lower than the deliverable supply: in accordance with Article 18 (3) of RTS 21, the other months' limit is therefore to be adjusted upwards.
25. All the other potential adjustment factors set out in RTS 21 have been considered and were 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 BaFin has not found evidence that this is excessive or that lower position limits would reduce volatility.
26. Based on the above, BaFin has decided to set a total upward adjustment of 10-percentage points resulting in an adjusted baseline of 35% of deliverable supply. This provides a figure of 11,793,135 MWh.

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

27. This Opinion concerns positions held in Spanish Power Futures and Options contracts.
28. ESMA has performed the assessment based on the information provided by BaFin.
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. The overall open interest in the EEX Spanish Power Futures and Options contracts amounts to 33,694,672 MWh, which translates into 46,798 lots.
31. When performing this assessment, ESMA also took into account the need to ensure that the methodology set out in RTS 21 promotes a consistent application of position limits across competent authorities including when commodity derivatives are based on the same underlying such as Spanish power in this case.

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

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



Spot month position limit

33. The deliverable supply was estimated based on ENTSO-E (European Network of Transmission System Operators for Electricity) data. It is composed of the average Spanish domestic Net Generating Capacity (NGC) and Spain yearly power import capacity for the year 2020. ESMA agrees with using data from ENTSO-E data to calculate deliverable supply as this ensures publicly available figures consistent at the European level.

34. ESMA considers that the methodology used to calculate deliverable supply is consistent with Article 10(1) of RTS 21 that sets out that deliverable supply shall be calculated “by identifying the quantity of the underlying commodity that can be used to fulfil the delivery requirements of the commodity derivative.”

35. The monthly deliverable supply figure has been calculated by converting the capacity (expressed in MW) to MWh per month.

36. 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”.

37. ESMA agrees that the rationale underpinning Article 18(3) of RTS 21 with respect to the spot month enables the national competent authority to adjust the spot month limit downwards in case the deliverable supply is significantly higher than the open interest. ESMA therefore considers that a downward adjustment of the spot month limit for the Spanish power Future contracts is reasonable under Article 18(3) of RTS 21.

#### Other months' position limit

38. The open interest has been calculated by BaFin based on position reporting data where the daily net positions have been added up and divided by the factor 2 ("net approach"). The number provided is the average size of daily open interest from December 2019 till end of November 2020. ESMA considers that such calculation of open interest by the competent authority provides the most accurate and reliable figure and promotes convergence in the setting of position limits by competent authorities. ESMA also considers such approach consistent with Article 12 of RTS 21.
39. ESMA considers that the adjustment made under Article 16 of RTS 21 is appropriate given the large number of separate expiries.
40. The other months' limit has been adjusted upwards to take into consideration the fact that the amount of open interest is significantly lower than the deliverable supply. This is consistent with Article 18(3) of RTS 21.
41. Consequently, these position limits have been set following the methodology established by RTS 21.
42. ESMA also notes that, overall, the position limits set result in a consistent and harmonised approach in the application of position limits for derivatives contracts based on Spanish power.

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

43. Under Article 57(1) of MiFID II, the objectives of the position limits are to prevent market abuse and support orderly pricing and settlement conditions including preventing market distorting positions.
44. With respect to the spot month limit, ESMA notes, based on the information provided by the competent authority, that the limit is substantially higher than open interest in the spot month throughout 2020.
45. ESMA understands the need to avoid the risk of unduly constraining trading in this commodity derivative market where underlying market participants have a key presence. However, there is a risk that the objectives set out in Article 57(1) of MiFID II may not be



achieved where the limit set for the spot month is well above the positions held by market participants in the spot month

46. In light of the assessment above, ESMA considers that the position limit set for the spot month and the other months, overall 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 commodity market and the liquidity of the EEX Spanish Power Base contracts are not hampered
47. However, to help ensure that the risk of not achieving the objectives set out in Article 57(1) of MiFID II does not materialise, ESMA considers that trading patterns in the EEX Spanish Power Base contracts should be carefully monitored by the competent authority, in particular during the spot month, and that the spot month limit should be reviewed on a timely basis.

## **VI. Conclusion**

48. 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,

Steven Maijoor

Chair

For the Board of Supervisors