European Securities and Markets Authority

Date: 24 June 2021
ESMA70-155-12003

OPINION on position limits on EEX TTF gas contracts

I. Introduction and legal basis

1. On 2 June 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[1] ("MiFID II"). The notification is regarding the exact position limits BaFin intends to 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.

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.

3. On 2 September 2020, ESMA issued an Opinion regarding the exact position limits BaFin intended to set for the Dutch Title Transfer Facility ("TTF") Gas futures and options commodity contracts. The position limits considered by BaFin in September 2020 was 52,466,250 MWh for the spot month limit and 112,196,688 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 again the open interest at the beginning of year 2021 based on position reporting data. BaFin considered that there had been a decrease in the open interest compared to its initial submission and that that the

[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).

position limits for both the spot month and the other months had therefore to be reconsidered. ESMA understands that the new position limits will apply after 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 Dutch TTF 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: natural gas (NGAS)

Commodity further sub product: TTF (TTFG)

Name of trading venue: EUROPEAN ENERGY EXCHANGE

MIC: XEEE

Venue product codes: G3B, O3B

III. Market description

6. 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.

7. 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.

8. 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.

9. 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. 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. According to the Herfindahl-Hirschman-Index there is no evidence of a dominant position in the Dutch gas market.

10. 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 do not have a shipper or supply agreement in the market (banks, commodities traders, investment firms, …).

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

12. 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. It was abstained from applying a decreasing position limit or a downward adjustment due to short maturities as a monthly contract of 720 MWh is the minimum tradeable amount.

IV. Proposed limit and rationale

Spot month position limit

<u>Deliverable supply calculation methodology</u>

13. Deliverable supply amounts to 219,735,000 MWh.

14. 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.

15. This calculation takes into account the following sources:

1) Entry pipeline capacity (2020) = 1,154 GWh/d[4]

2) Imports (2020) = 1,381 GWh/d[5] (LNG=418 GWh/d and 963 GWh/d imports from Norway)

3) Storage withdrawal capacity (2018) = 3,728.5 GWh/d[6]

4) Indigenous production (2019) = 1,061 GWh/d[7]

16. The total deliverable supply sums up to 7,324.5 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 7,324,500 MWh per day. To obtain the monthly capacity, the capacity in MWh per day needs to be multiplied by 30.

Spot month position limit

17. Spot month limit amounts to 54,933,750 MWh, which corresponds to 25% of the deliverable supply. The limit applies to EEX TTF Gas futures and options contracts.

Spot month position limit rationale

18. 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% * 219,735,000 MWh = 54,933,750 MWh.

19. BaFin considered the following factor relevant for adjusting the limit upwards from the baseline:

-The TTF Gas futures contracts are all physically settled and thereby result in an actual physical flow of gas. Market participants active in the physical gas market who operate facilities with substantial generation/storage capacity or large demand assets, can have a natural relatively large position in the gas derivatives market. On the other hand, only a few utility firms act as liquidity provider. This needs to be taken into account under Article 20 (2) (d) of RTS 21) in relation to the composition and role of market participants on the underlying commodities.

20. BaFin considered the following factor relevant for adjusting the limit downwards from the baseline:

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4 https://www.entsog.eu/sites/default/files/2021-01/ENTSOG_GIE_SYSDEV_2019-2020_1600x1200_FULL_047.pdf
5 Source: https://www.entsog.eu/sites/default/files/2021-01/ENTSOG_GIE_SYSDEV_2019-2020_1600x1200_FULL_047.pdf
6 http://www.gie.eu/index.php/maps-data/gse-storage-map
https://www.gie.eu/index.php/gie-publications/databases/storage-database
7 Eurostat: http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=nrg_103m&lang=en

-Deliverable supply: Gas delivered in the Dutch market area as underlying is also used as the deliverable supply for other commodity derivatives in the EU, for instance at ICE Endex (Article. 17 of Commission Delegated Regulation (EU) 2017/591);

21. 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.

22. Overall, taking into account the upward and downward adjustment factors, BaFin has set the spot month limit at 25% of deliverable supply which provides a figure of 54,933,750 MWh.

Other months' position limit

Open interest calculation methodology

23. The open interest amounts to 179,274,678 MWh.

24. The open interest value was calculated throughout the period from April 2020 to February 2021. The open interest for these contracts[8] 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 throughout the relevant period. Option positions in options have been delta adjusted.

Other months' position limit

25. Other months limit amounts to 44,818,670 MWh, which corresponds to 25% of the open interest. The limit applies to EEX Dutch TTF gas futures and options contracts.

Other months' position limit rationale

26. The open interest amounts to 179,274,678 MWh. The baseline figure for the other months limit amounts to 25% of open interest, i.e. 44,818,670 MWh.

27. BaFin considered the following factor relevant for adjusting the limit upwards from the baseline:

-The TTF Gas futures contracts are all physically settled and thereby result in an actual physical flow of gas. Market participants active in the physical gas market who

[8] The open interest for the previous position limit was calculated by BaFin on basis of information received directly from the trading venue.

operate facilities with substantial generation/storage capacity or large demand assets, can have a natural relatively large position in the gas derivatives market. On the other hand, only a few utility firms act as liquidity provider. This needs to be taken into account under Article 20(2)(d) of RTS 21 in relation to the composition and role of market participants on the underlying commodities.

28. BaFin considered the following factor relevant for adjusting the limit downwards from the baseline:

-Deliverable supply: Gas delivered in the Dutch market area as underlying is also used as the deliverable supply for other commodity derivatives in the EU, for instance at ICE Endex (Art. 17 of Commission Delegated Regulation (EU) 2017/591).

29. 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.

30. Overall, taking into account the upward and downward adjustment factors, BaFin has set the other month limit at 25% of open interest which provides a figure of 44.818.670 MWh.

V. ESMA's Assessment

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

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

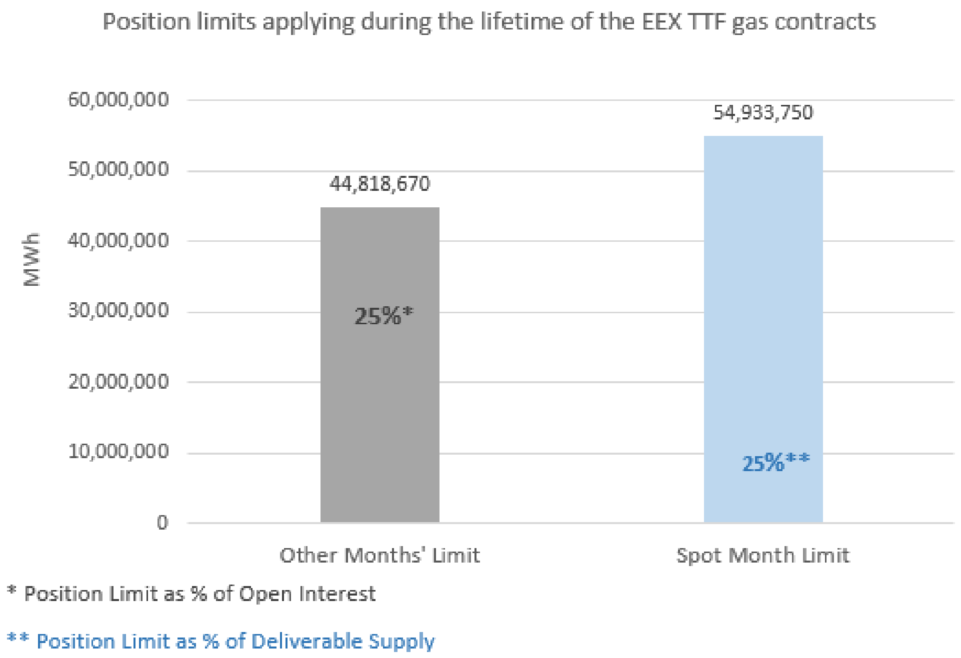
33. The overall open interest in the EEX TTF gas commodity derivatives amounts to 179,274,678 MWh, which translates into 248,993 lots. Since the level of open interest is above 20,000 lots, the spot month and the other months' limits can be set between 5% and 35% of the reference amount in accordance with Article 14 of RTS 21.

34. 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.

35. 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 TTF gas 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

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



Spot month position limit

37. The calculation of the deliverable supply is based on ENTSO-G 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.

38. ESMA notices that the calculation of available gas in storage includes the withdrawal rate from storages located in Germany that are directly and solely connected to the Dutch grid. ESMA agrees that adding to total storage capacity the withdrawal rates figures from German storages provides an adequate representation of natural gas in storage. Furthermore, ESMA agrees with using a figure that corresponds to the minimum between German storage withdrawal rate and border interconnector capacity, to take into account both restrictions.

39. These values of ENTSO-G have been converted from GWh/d to MWh. To do so the values in GWh/d have been converted to MWh/d, multiplying it by 1,000. To obtain the monthly capacity the resulting value has been multiplied by 30, resulting in a deliverable supply of 219,735,000 MWh.

40. 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".

41. ESMA considers that it is a reasonable approach to have adjusted the spot month limit upwards to take into consideration the composition and role of market participants in the underlying market in accordance with Article 20 (2)(d) of RTS 21.

42. ESMA also agrees that a downward adjustment is justified under Article 17 of RTS 21 due to the fact that the deliverable supply is also used as deliverable supply for other commodity derivatives.

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

43. 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 April 2020 to February 2021. 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.

44. ESMA considers that it is a reasonable approach to have adjusted the other months' limit upwards to take into consideration the composition and role of market participants in the underlying market in accordance with Article 20 (2)(d) of RTS 21.

45. ESMA also agrees that a downward adjustment is justified under Article 17 of RTS 21 due to the fact that the deliverable supply is also used as deliverable supply for other commodity derivatives.

46. 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

47. 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.

48. 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

49. 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, 24 June 2021

Tuominen Anneli 912372492

Anneli Tuominen

Interim Chair

For the Board of Supervisors