European Securities and Markets Authority

Call for evidence

Position limits and position management in commodity derivatives

24 May 2019 | ESMA70-156-1101

Responding to this paper

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex 1. Comments are most helpful if they:

- respond to the question stated;
- indicate the specific question to which the comment relates;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

ESMA will consider all comments received by **5 July 2019.**

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'. Please follow the instructions given in the document 'Reply form for the call for evidence on position limits and position management controls in commodity derivatives' also published on the ESMA website.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publically disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the heading Legal Notice.

Who should read this paper

All interested stakeholders are invited to respond to this consultation paper. This consultation paper is primarily of interest to trading venues, investment firms and non-financial counterparties trading in commodity derivatives, but responses are also sought from any other market participant including trade associations, industry bodies and investors.

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Acronyms used

CA	Competent Authority
CFTC	Commodity Futures Trading Commission
EEOTC	Economically Equivalent OTC Contracts
ESMA	European Securities and Markets Authority
EC	European Commission
EU	European Union
MAR	Regulation (EU) No596/2014 of the European Parliament and the Council of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC and Directives 2003/124/EC, 2003/125/EC and 2004/72/EC
MiFID I	Directive 2004/39 of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directive 85/611/EC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC
MiFID II	Directive 2014/65/EU of the European Parliament and 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)
MiFIR	Regulation (EU) No 600/2014 of the European Parliament and of the Council on markets in financial instruments and amending Regulation (EU) No 648/2012 (OJ L 173, 12.6.2014, p. 84)
OTC	Over-the-counter
REMIT	Regulation (EU) No 1227/2011of the European parliament and of the Council of 25 October 2011 on wholesale energy market integrity and transparency
RTS 21	Commission Delegated Regulation (EU) 2017/591 of 1 December 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 to commodity derivatives

1 Executive Summary

Reasons for publication

Under Article 90(1) of MiFID II, “Before 3 March 2020, the Commission shall, after consulting ESMA, present a report to the European Parliament and the Council on […] (f) the impact of the application of position limits and position management on liquidity, market abuse and orderly pricing and settlement conditions in commodity derivatives markets; […].”

Based on a revised timeline agreed with the European Commission (EC), ESMA will be delivering its advice to the Commission’s report on the impact of position limits and position management on commodity derivatives markets by 31 March 2020. This call for Evidence is a first step to that end. It is issued to seek the views and input of stakeholders on the impact of position limits and position management controls in commodity derivatives markets. It further aims at gathering views on potential amendments to the existing regime that may be considered appropriate based on the experience gathered so far.

Contents

Section 3 of the call for evidence provides a summary of the position limit regime under MiFID II and seeks stakeholders’ views on the potential impact of position limits on liquidity, market abuse and orderly pricing and settlement conditions in commodity derivatives markets. Section 4 discusses the impact of position management controls on commodity derivatives markets. Section 5 takes a forward-looking perspective and considers potential improvements to the existing framework

Next Steps

ESMA will consider the feedback to this call for evidence to draft its advice to the EC’s Report on the impact of position limits and position management controls on commodity derivatives markets. Then, ESMA will consult on a draft report in the last quarter of 2019 with a view to finalising the report by the end of March 2020.

2 Introduction

1. In response to the 2009 Pittsburgh G20 summit's agreement to improve the regulation, functioning and transparency of financial and commodity derivative markets and the 2011 Cannes G20 summit's call for market regulators to have formal position management powers, MiFID II introduced a new set of provisions governing trading in commodity derivative markets. Those commodity derivative provisions are one of the key changes in MiFID II compared to MiFID I.

2. In addition to pre-trade and post-trade transparency as well as transaction reporting requirements, MiFID II introduces a position limit, a position reporting and a position management regime for commodity derivatives. As it is common for newly introduced provisions, under Article 90(1)(f) of MiFID II the co-legislators have asked the Commission, after consulting ESMA, to present a report to the European Parliament and to the Council on "the impact of the application of position limits and position management on the liquidity, market abuse and orderly pricing and settlement conditions in commodity derivatives markets".

3. Since the entry into application of the new commodity derivatives framework, ESMA has received only partial feedback from stakeholders on the impact of position limits and position management controls. ESMA has therefore decided to issue a call for evidence before consulting on a draft report, noting that it is not intended to replicate these two rounds of consultations for the other reports to be delivered by ESMA under MiFID II/MiFIR. Through this call for evidence, ESMA is seeking the input of stakeholders to form a more exhaustive and informed view on the issues to be considered and addressed in the advice to the Commission. In particular, stakeholders are invited to share their experience with the application of the MiFID II position limit and position management provisions, explain how trading in commodity derivatives may have been impacted, either positively or negatively, by this new regime and provide thoughts for potential amendments.

4. Section 3 of the call for evidence seeks stakeholders' views on the potential impact of position limits on liquidity, market abuse and orderly pricing and settlement conditions in commodity derivatives markets. Section 4 discusses the impact of position management controls thereon. Finally, Section 5 takes a forward-looking perspective and seeks views on potential improvements to the existing framework.

3 MiFID II position limits

3.1 Summary of the MiFID II position limit regime

5. Under Article 57(1) of MiFID II, Competent Authorities (CAs) have to establish and apply position limits on the size of a net position which a person can hold at all times in commodity derivatives traded on trading venues and in economically equivalent OTC

(EEOTC) contracts. The limits apply to all positions held by a person and those held on its behalf at an aggregate group level.

6. The position limits must be set so as to prevent market abuse and support orderly pricing and settlement conditions, including preventing market distorting positions, and ensuring, in particular, convergence between prices of derivatives in the delivery month and spot prices for the underlying commodity, without prejudice to price discovery on the market for the underlying commodity.

7. Position limits do not apply to positions held by, or on behalf of, non-financial entities and which are objectively measurable as reducing risk directly related to the commercial activity of that non-financial entity where that non-financial entity has applied for an exemption in accordance with Article 8 of RTS 21.

8. Position limits apply to all commodity derivatives traded on a trading venue, whatever the underling commodity and whether the derivative contract is physically or cash settled. Position limits also apply to securitised derivatives which relate to a commodity or an underlying referred to in Section C(10) of Annex I of MiFID II. As regards derivatives based on C(10) underlyings, ESMA clarified in its Q&As on MiFID II commodity derivatives topics that position limits should only apply to freight rate derivatives (wet and dry freight) and to derivative contracts relating to indices if the underlying index is materially based on commodity underlyings. ESMA considers that the underlying index is materially based on commodities if such commodities have a weighting of more than 50% in the composition of the underlying index.1

[1] https://www.esma.europa.eu/sites/default/files/library/esma70-872942901-36_qas_commodity_derivatives.pdf

Definition of commodity derivatives

MIFIR

<u>*Article 2(1)(30):*</u> *commodity derivatives' means those financial instruments defined in point (44)(c) of Article 4(1) of Directive 2014/65/EU; which relate to a commodity or an underlying referred to in Section C(10) of Annex I to Directive 2014/65/EU; or in points (5), (6), (7) and (10) of Section C of Annex I thereto;*

MiFID II

<u>*Article 4(1)(44)(c):*</u> *any other securities giving the right to acquire or sell any such transferable securities or giving rise to a cash settlement determined by reference to transferable securities, currencies, interest rates or yields, commodities or other indices or measures*

<u>*Annex I Section C*</u>

[…]

(5) Options, futures, swaps, forwards and any other derivative contracts relating to commodities that must be settled in cash or may be settled in cash at the option of one of the parties other than by reason of default or other termination event;

(6) Options, futures, swaps, and any other derivative contract relating to commodities that can be physically settled provided that they are traded on a regulated market, a MTF, or an OTF, except for wholesale energy products traded on an OTF that must be physically settled;

(7) Options, futures, swaps, forwards and any other derivative contracts relating to commodities, that can be physically settled not otherwise mentioned in point 6 of this Section and not being for commercial purposes, which have the characteristics of other derivative financial instruments;

[…]

(10) Options, futures, swaps, forward rate agreements and any other derivative contracts relating to climatic variables, freight rates or inflation rates or other official economic statistics that must be settled in cash or may be settled in cash at the option of one of the parties other than by reason of default or other termination event, as well as any other derivative contracts relating to assets, rights, obligations, indices and measures not otherwise mentioned in this Section, which have the characteristics of other derivative financial instruments, having regard to whether, inter alia, they are traded on a regulated market, OTF, or an MTF;

[…].

9. Position limits do not apply to physically-settled wholesale energy products traded on an Organised Traded Facility (OTF). Under Annex I, Section C(6) of MiFID II, those products do not qualify as financial instruments and therefore are outside the scope of MiFID II. Wholesale energy products are defined by reference to Article 2(4) of REMIT, which refers to "[…] derivatives related to electricity or natural gas produced, traded or delivered in the Union […]."

10. The position limits must be set by the CA so as to prevent market abuse and support orderly pricing and settlement conditions. In addition, the position limits set by the CA for the spot month and the other months have to comply with the methodology set out in RTS 21. Whilst Article 57(3) of MiFID II provides a list of factors to be taken into account by CAs when setting the position limits, RTS 21 further clarifies how those factors may be used by CAs to adjust the position limit upwards or downwards compared to a set baseline. RTS 21 also provides for default or "*de minimis*" position limits for new and illiquid contracts that do not reach a minimum level of open interest over a consecutive three-month period.

11. CAs must notify ESMA of the position limits they intend to set for derivative contracts, except for derivative contracts with de minimis position limits under RTS 21, and ESMA must issue an opinion assessing the compatibility of the position limits with the objective of preventing market abuse and supporting orderly pricing and settlement conditions and with the requirements established in RTS 21. As of 2 May 2019, ESMA has issued 38 opinions.

3.2 Impact of positions limits on liquidity

12. The first part of the mandate in Article 90(1)(f) of MiFID II asks ESMA to report on the impact of the position limit regime on the liquidity of commodity derivative markets. ESMA so far has limited evidence as to whether position limits have had an impact on the criteria typically used to assess liquidity such as spreads or market depth and is seeking information from stakeholders on their assessment of how liquidity has changed since 3 January 2018.

13. Based on the data gathering exercise ESMA conducted to update its Opinion on Ancillary Activity Calculations, ESMA noted that trading volumes in commodity derivatives on EU trading venues have increased in almost all commodity derivatives asset classes in 2018 compared to 2017.

14. Increase in EU trading volume has been more significant in gas, power and emission allowances whereas trading in agriculture derivatives and C(10) derivatives slightly decreased. With Brexit in mind, it is worth noting that there is still no trading taking place in metal, oil and coal contracts on EU27 trading venues or only in minimum volume. In all commodity derivatives asset classes except power and C(10) derivatives, on-venue trading concentrates on UK trading venues.

15. ESMA is aware of one concern from stakeholders regarding the default position limit of 2,500 lots set out in Article 15(1) of RTS 21 for new and illiquid contracts with a total combined open interest in spot and other months' contracts not exceeding 10,000 lots over a consecutive three-month period. Stakeholders have reported that this provision may not allow the development of recently launched contracts.

16. Taking into consideration the concerns expressed, ESMA has clarified in its Q&As on MiFID II commodity derivatives topics that for those contracts with a total combined open interest in spot and other month's contracts exceeding 5,000 lots over a consecutive three month period, and where the automatic limit under Article 15(1)(a) would unduly constrain the operation of the market and prevent the contract from supporting the functioning of commercial activities in the underlying market, the CA may set the position limits within the range established by Article 19(2) of RTS 21, i.e. between 5% and 50% of the reference amount.

17. ESMA is seeking input on other possible ways of allowing for the adequate development of new and illiquid contracts within the MiFID II framework.

Q1 In your view, what impact, if any, did the introduction of position limits have on the availability and liquidity of commodity derivative markets? What are in your views the main factors driving this development, e.g. the mere existence of a position limit and position reporting regime, some specific characteristics of the position limit regime or the level at which position limits are set? Please elaborate by differentiating per commodity asset class or contract where relevant and provide evidence to support your assessment.

Q2 Have you identified other structural changes in commodity derivative markets or in the underlying markets since the introduction of the MiFID II position limit regime, such as changes in market participants? If so, please provide examples, and where available data, and differentiate per commodity derivative asset class where relevant.

3.3 Impact of positions limits on market abuse

18. Under Article 57(1) of MiFID II, one of the objectives to be met by the position limits set by the relevant CA is to "prevent market abuse."

19. Under the Market Abuse Regulation (MAR), the definition of market abuse comprises practices such as insider dealing, unlawful disclosure of inside information and market manipulation.

20. In general, a position reporting regime may help to identify the build-up of concentration of positions, which in turn could prove possible market abuse. Position limits may cap the financial gain a market participant could potentially make when unlawfully taking advantage of inside information or when manipulating the market in a commodity derivative contract, thereby rendering such abusive practices less attractive. However,

that rather appears as an indirect potential consequence of the position limits set rather than a means of preventing market abuse in its own right.

21. More specifically in relation to market manipulation, Article 12(1) of MAR stipulates that market abuse “shall comprise […]

a) entering into a transaction, placing an order to trade or any other behaviour which

i) gives, or is likely to give, false or misleading signals as to the supply of, demand for, or price of, a financial instrument, a related spot commodity contract […]; or

ii) secures or is likely to secure the price of one or more financial instruments, a related spot commodity contract […] at an abnormal or artificial level”;

b) entering into a transaction, placing an order to trade or any other activity or behaviour which affects or is likely to affect the price of one or several financial instruments, a related spot commodity contract […] which employs a fictitious device or any other form of deception or contrivance;”

22. However, whereas some characteristics of a commodity derivative contract, such as whether the index used for settlement is a reliable one or whether the deliverable supply in the underlying commodity can be restricted or controlled, contribute to making the contract more or less readily susceptible to manipulation, the extent to which position limits contribute to preventing market abuse appears less apparent.

Q3 Do you consider that position limits contribute to the prevention of market abuse in commodity derivatives markets? Please elaborate by differentiating per behaviour, per commodity asset classes or contract where relevant and provide evidence to support your assessment when available.

3.4 Impact of positions limits on orderly pricing and settlement conditions

23. Under point (b) of Article 57(1), position limits must be set in order to support “orderly pricing and settlement conditions, including preventing market distorting positions, and ensuring, in particular, convergence between prices of derivatives in the delivery months and spot prices for the underlying commodity, without prejudice to price discovery on the market for the underlying commodity”.

24. As stated in the 2011 IOSCO Principles for the Regulation and Supervision of Commodity Derivatives Markets[2], “With respect to derivatives markets, an orderly market may be characterised by, among other things, parameters such as a rational relationship between

[2]https://www.iosco.org/library/pubdocs/pdf/IOSCOPD358.pdf

consecutive prices, a strong correlation between price changes and the volume of trades, accurate relationships between the price of a derivative and the underlying commodity and reasonable spreads between near and far dated contracts. Numerous conditions can negatively affect trading and the characteristics of an orderly market, […] including unmanaged imbalance between long and short positions resulting from large concentrated positions."

25. Position limits are a means to address the potential for large positions in commodity futures and options markets to prejudice orderly market functioning. This is because the capacity of a market to absorb the establishment and liquidation of large positions in an orderly manner is related to the size of such positions relative to the market.

26. Spot month positions limits in particular are important to support orderly pricing and settlement conditions. As further explained in Recital (11) of RTS 21 with regards to the spot month limit, "Restricting the positions a person may hold in the period during which the physical delivery is to be made limits the quantity of the underlying deliverable supply each person may make or take delivery of, thereby preventing the accumulation of dominant positions by individuals, which may enable them to squeeze the market through restricting access to the commodity". Recital (11) of RTS 21 also clarifies that CAs have the possibility "to implement a schedule of decreasing position limits ranging from the point in time when a contract becomes a spot month contract until maturity in order to more precisely ensure that position limits are adequately set throughout the spot month period and to ensure orderly settlement".

27. When reviewing the position limits submitted by CAs, ESMA however noted that only one CA made use of decreasing or gliding-path position limits throughout the spot month for agricultural commodity derivatives with one limit applying for the first part of the spot month and a reduced one applying during the last 12 days of the spot month. Another CA did not set different limits across the spot month but is relying on the more stringent position limit set by the trading venue for some contracts as part of its position management powers for the period immediately preceding delivery to ensure orderly pricing and settlement conditions.

28. ESMA also notes that under the methodology set out in RTS 21, and with the exception of securitised commodity derivatives, the spot month limit is based on available deliverable supply for the underlying commodity. Where there is a significant difference between deliverable supply and open interest in the spot month for a specific contract, even a spot month limit set at the lowest possible percentage of the deliverable supply (5%) may remain far above the spot month open interest and does not have any impact on orderly pricing and settlement conditions. On the other hand, it may also be argued that when deliverable supply is significantly higher than open interest during the spot month, there is no need to restrict trading to address potential risks to orderly pricing and settlement conditions when the contract approaches expiration.

29. Finally, and as recalled earlier, MiFID II position limits apply equally to physically settled and cash settled contracts. Whilst, depending on the characteristics of the contract and

the underlying market, potential risks to orderly pricing and settlement conditions may become all the more significant when a physically settled contract is coming close to expiry, risks also exist for cash settled contracts where the position holder would have the capacity to influence the price of the underlying. Spot month limits may then reduce the incentive, and potential benefit, to do so.

Q4 In your view, what impact do position limits have on the orderly pricing and orderly settlement of commodity derivative contracts? Please elaborate by differentiating per asset class or per contract where relevant and provide evidence to support your answer when available

Q5 More generally, and beyond the specific items identified above, what would be your overall assessment of the impact of position limits on EU commodity derivatives markets since the application of MiFID II?

4 MiFID II Position management

4.1 The MiFID II Position management regime

30. Under Article 57(8) of MiFID II, "Member States shall ensure that an investment firm or a market operator operating a trading venue which trades commodity derivatives apply position management controls. Those controls shall include at least, the powers for the trading venue to:

(a) monitor the open interest positions of persons;

(b) access information, including all relevant documentation, from persons about the size and purpose of a position or exposure entered into, information about beneficial or underlying owners, any concert arrangements, and any related assets or liabilities in the underlying market;

(c) require a person to terminate or reduce a position, on a temporary or permanent basis as the specific case may require and to unilaterally take appropriate action to ensure the termination or reduction if the person does not comply; and

(d) where appropriate, require a person to provide liquidity back into the market at an agreed price and volume on a temporary basis with the express intent of mitigating the effects of a large or dominant position."

31. Information on position management controls in place at commodity derivatives trading venues is available on ESMA's website[3]. In most cases, the information provided explains with a varying degree of detail, how the position management controls in place achieve

[3] this information is available on ESMA website https://www.esma.europa.eu/sites/default/files/library/position_management_controls.xlsx

compliance with the Article 57(8) requirements. However, two trading venues have mentioned position management controls that extend beyond the ones set out in Article 57(8) of MFID II. ICE Futures Europe may promulgate limits and associated arrangements in relation to open positions that may be owned, controlled or carried by a Member or Person for his own account or for another Person. The London Metal Exchange (LME) has introduced a requirement for the provision of additional information upon request, for positions held by Members either directly or on behalf of their Client(s) that are above the Accountability levels set by the venue for each contract code.

32. ESMA has no indication that position management controls by trading venues have had an impact on the liquidity of commodity derivatives markets and would therefore very much welcome stakeholders on this issue.

Q6 Do you consider that position management controls have an impact on the liquidity of commodity derivatives markets? If so, please elaborate, differentiating per commodity derivative trading venues or contract where appropriate.

33. As regards market abuse, ESMA's preliminary views would be that position management controls are a relevant means available to trading venues to help detect and potentially deter unfair trading practices. Where position management controls include the setting of ex-ante position limits, including around the delivery period, they further contribute to orderly pricing and settlement conditions.

34. Position management controls in relation to commodity derivatives may also be considered in conjunction with the broader obligation for trading venues to establish and maintain effective arrangements, systems and procedures aimed at preventing and detecting insider dealing, market manipulation and attempted insider dealing and market manipulation under Article 16(1) of MAR.

Q7 Do you consider that position management controls adopted by commodity derivative trading venues contribute to the prevention of market abuse? If so, please elaborate, differentiating per commodity derivative trading venues or contract where appropriate.

Q8 Do you consider that position management controls adopted by commodity derivative trading venues have a role on orderly pricing and settlement conditions? If so, please elaborate, differentiating per commodity derivative trading venues or contract where appropriate.

Q9 If you are a commodity derivative trading venue, please explain how you have been exercising your position management controls since MiFID II application. In particular, how frequently did you ask further information on the size or purpose of a position, on beneficial owners or assets and liabilities in the underlying commodity under Article 57(1)(b) of MiFID II, require a person to terminate or reduce a position under Article 57(1)(c) of MiFID II, require a person

to provide liquidity back into the market under Article 57(1)(d) of MiFID II or exercise any of your additional position management controls?

5 Way forward

35. Almost 18 months after the start of the application of the MiFID II position limit and position management regime, and in addition to assessing whether the new framework has delivered on the objectives identified, ESMA considers that it would also be useful to seek stakeholders' views as to whether some amendment to the Level 1 or Level 2 provisions could improve the overall efficiency of the new framework. The section below includes a non-exhaustive list of topics for discussion.

36. ESMA also notes that the landscape of EU commodity derivative trading is expected to change significantly when the UK leaves the EU as some commodity derivative asset classes may no longer be traded on EU venues, or only marginally. ESMA is of the view that this may ultimately require a change to the quantitative approach set out in Level 1 for the ancillary activity test and the consequent scope of entities able to use to use the position limit exemption.

Q10 Do you have any general comment on the position limit regime and associated position reporting introduced by MiFID II?

Q11 In your view, how will EU commodity derivatives markets be impacted by the UK leaving the EU? What consequences do you expect from Brexit on the commodity derivatives regime under MiFID II?

5.1 Position limits

5.1.1 Commodity derivatives under the scope of the position limit regime

37. As recalled earlier, the MiFID II position limit regime has a broad scope and encompasses all commodity asset classes as well as all types of commodity derivative contracts, be they cash settled or financially settled, new and illiquid contracts or more mature ones.

38. ESMA notes in particular that according to Article 2(1)(30) of MiFID II, the definition of commodity derivatives includes securitised derivatives. However, the notions of spot month and other months, for which position limits are to be set under Article 57(3) of MiFID II are not relevant for securitised derivatives. The concept of open interest does not apply either to those instruments in a straightforward manner and ESMA had to find a meaningful approach to position limits in securitised derivatives in Article 15 pf RTS 21.

39. As regards third-country position limit regimes, the UK has on-shored the MiFID II position limit framework to be implemented when the UK leaves the EU. However, ESMA notes that, by contrast to the MiFID II regime, the Commodity Futures Trading Commission (CFTC) position limits currently apply only to a limited set of nine agricultural contracts and

is of the view that there could be merits in limiting the application of MiFID II position limits II to a more limited set of important, critical commodity derivative contracts.

Q12 Taking into consideration the intended purposes of position limits, do you consider that they deliver the same benefit across all commodity asset classes and across all types of commodity derivatives? Please explain.

Q13 Would you see benefits in limiting the application of position limits to a more limited set of commodity derivatives? If so, to which ones and on which criteria?

Q14 More specifically, are you facing any issue with the application of position limits to securitised derivatives? If so, please elaborate.

40. In order to avoid circumvention, position limits also apply to EEOTC contracts, as further defined in Article 6 of RTS 21 which sets out that "An OTC derivative shall be considered economically equivalent to a commodity derivative traded on a trading venue where it has identical contractual specifications, terms and conditions, excluding different lot size specifications, delivery dates diverging by less than one calendar day and different post trade risk management arrangements." However, ESMA notes that very few EEOTC contracts appear to have been identified by market participants.

Q15 Do you consider that there would be merits in reviewing the definition of EEOTC contracts? If so, please explain the changes you would suggest.

5.1.2 Exemptions

41. Position limits do not apply to positions held by or on behalf of a non-financial entity and which are objectively measurable as reducing risks directly relating to the commercial activity of that non-financial entity[4], provided that the non-financial entity has applied for the exemption from position limits in accordance with Article 8 of RTS 21. In contrast, position limits apply to market makers and other market participants providing liquidity to non-financial entities. ESMA notes that some CAs have adjusted position limits upwards compared to the baseline to allow such market participants to fulfil their liquidity provision activity. ESMA also notes that in some cases, position limits have been adjusted upwards to take into account the positions held by third-country non-financial counterparties reluctant to apply for an exemption.

Q16 In your view, would there be a need to review the MiFID II position limit exemptions? If so, please elaborate and explain which changes would be desirable.

[4] As further defined in Article 7 of RTS 21

5.1.3 Methodology for setting position limits

42. Based on the experience gathered when reviewing position limits, ESMA would see room for improvements in the RTS 21 methodology as the methodology was initially drafted without having possibly in mind all existing contract specifications, underlying market particularities or trading environment characteristics.

43. ESMA noted in particular that the current methodology may not be best fitted to deal with commodity derivatives contracts that are cash settled, including cash settled contracts based on indices. For those types of contracts, deliverable supply may not appear as the most relevant reference amount for calculating the spot month limit, notably where there is a significant difference between deliverable supply in the underlying commodity and the amount of open positions. In such circumstances, and to ensure that RTS 21 allows for the setting of meaningful position limits, there could be value in providing the relevant CA with the possibility to use open interest as a reference for both the spot month and the other month's limits.

Q17 Would you see merits in the approach described above and the additional flexibility provided to CAs for setting the spot month limit in cash settled contracts? Please explain.

44. ESMA is considering other potential amendments to RTS 21 that it may include in its advice to the EC and welcomes contributions from stakeholders in this area.

Q18 Would you see benefits to review the approach for setting position limits for new and illiquid contracts? If so, what would you suggest?

Q19 Would you see merits in a more forward-looking approach to the calculation of open interest used as a baseline for setting position limits? Please elaborate.

Q20 In your view, are there other specific areas where the methodology for calculating the position limits set out in RTS 21 should be reviewed? If so, what would you suggest, and why?

5.2 Position management controls

45. So far, ESMA has received limited feedback on the application of the provisions on position management controls by trading venues and market participants. Therefore, ESMA would welcome any suggestion aiming at improving the existing framework.

Q21 How useful do you consider the information on position management controls available on ESMA's website[5]?

[5] https://www.esma.europa.eu/sites/default/files/tpeo_tullett_prebon_europe_otf_position_management_controls_20171221_0.pdf

Q22 Do you consider that there is a need to review the list of minimum position management controls to be implemented by commodity derivatives trading venues under Article 57(8) of MiFID II? If so, please explain the changes you would suggest.

6 Annex

Summary of questions

Q1 In your view, what impact, if any, did the introduction of position limits have on the availability and liquidity of commodity derivative markets? What are in your views the main factors driving this development, e.g. the mere existence of a position limit and position reporting regime, some specific characteristics of the position limit regime or the level at which position limits are set? Please elaborate by differentiating per commodity asset class or contract where relevant and provide evidence to support your assessment.

Q2 Have you identified other structural changes in commodity derivative markets or in the underlying markets since the introduction of the MiFID II position limit regime, such as changes in market participants? If so, please provide examples, and where available data, and differentiate per commodity derivative asset class where relevant.

Q3 Do you consider that position limits contribute to the prevention of market abuse in commodity derivatives markets? Please elaborate by differentiating per conduct, per commodity asset classes or contract where relevant and provide evidence to support your assessment when available.

Q4 In your view, what impact do position limits have on the orderly pricing and orderly settlement of commodity derivative contracts? Please elaborate by differentiating per asset class or per contract where relevant and provide evidence to support your answer when available.

Q5 More generally, and beyond the specific items identified above, what would be your overall assessment of the impact of position limits on EU commodity derivatives markets since the application of MiFID II?

Q6 Do you consider that position management controls have an impact on the liquidity of commodity derivatives markets? If so, please elaborate, differentiating per commodity derivative trading venues or contract where appropriate.

Q7 Do you consider that position management controls adopted by commodity derivative trading venues have a role on the prevention of market abuse? If so, please elaborate, differentiating per commodity derivative trading venues or contract where appropriate.

Q8 Do you consider that position management controls adopted by commodity derivative trading venues have a role on orderly pricing and settlement conditions? If so, please elaborate, differentiating per commodity derivative trading venues or contract where appropriate.

Q9 **If you are a commodity derivative trading venue, please explain how you have been exercising your position management controls since MiFID II application. In particular, how frequently did you ask further information on the size or purpose of a position, on beneficial owners or assets and liabilities in the underlying commodity under Article 57(1)(b) of MiFID II, require a person to terminate or reduce a position under Article 57(1)(c) of MiFID II, require a person to provide liquidity back into the market under Article 57(1)(d) of MiFID II or exercise any of your additional position management controls?**

Q10 **Do you have any general comment on the position limit regime and associated position reporting introduced by MiFID II?**

Q11 **In your view, how will EU commodity derivatives markets be impacted by the UK leaving the EU? What consequences do you expect from Brexit on the commodity derivatives regime under MiFID II?**

Q12 **Taking into consideration the intended purposes of position limits, do you consider that they deliver the same benefit across all commodity asset classes and across all types of commodity derivatives? Please explain.**

Q13 **Would you see benefits in limiting the application of position limits to a more limited set of commodity derivatives? If so, to which ones and on which criteria?**

Q14 **More specifically, are you facing any issue with the application of position limits to securitised derivatives? If so, please elaborate.**

Q15 **Do you consider that there would be merits in reviewing the definition of EEOTC contracts? If so, please explain the changes you would suggest.**

Q16 **In your view, would there be a need to review the MiFID II position limit exemptions? If so, please elaborate and explain which changes would be desirable.**

Q17 **Would you see merits in the approach described above and the additional flexibility provided to CAs for setting the spot month limit in cash settled contracts? Please explain.**

Q18 **Would you see benefits to review the approach for setting position limits for new and illiquid contracts? If so, what would you suggest?**

Q19 **Would you see merits in a more forward-looking approach to the calculation of open interest used as a baseline for setting position limits? Please elaborate.**

Q20 **In your view, are there other specific areas where the methodology for calculating the position limits set out in RTS 21 should be reviewed? If so, what would you suggest, and why?**

Q21 How useful do you consider the information on position management controls available on ESMA's website?

Q22 Do you consider that there is a need to review the list of minimum position management controls to be implemented by commodity derivatives trading venues under Article 57(8) of MiFID II? If so, please explain the changes you would suggest.