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| Response Form to the Consultation Paper |
| **Technical standards for commodity derivatives** |

**Responding to this paper**

ESMA invites comments on all matters in this consultation paper and in particular on the specific questions summarised in Annex I. 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 **23 July 2021.**

All contributions should be submitted online at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading ‘Your input - Consultations’.

**Instructions**

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the below steps when preparing and submitting their response:

1. Insert your responses to the questions in the Consultation Paper in the present response form.
2. Please do not remove tags of the type <ESMA\_QUESTION\_CD\_1>. Your response to each question has to be framed by the two tags corresponding to the question.
3. If you do not wish to respond to a given question, please do not delete it but simply leave the text “TYPE YOUR TEXT HERE” between the tags.
4. When you have drafted your response, name your response form according to the following convention: ESMA\_PFG\_nameofrespondent\_RESPONSEFORM. For example, for a respondent named ABCD, the response form would be entitled ESMA\_PFG\_ABCD\_RESPONSEFORM.
5. Upload the form containing your responses, in Word format, to ESMA’s website ([www.esma.europa.eu](http://www.esma.europa.eu) under the heading “Your input – Open consultations” 🡪 “Consultation on Position limits and position management in commodities derivatives”).

**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](http://www.esma.europa.eu) under the heading [Legal Notice](http://www.esma.europa.eu/legal-notice).

**Who should read this paper**

This document will be of interest to asset managers managing retail funds and their trade associations, as well as institutional and retail investors investing into such funds and their associations.

**General information about respondent**

|  |  |
| --- | --- |
| Name of the company / organisation | Commodity Markets Council Europe |
| Activity | Non-financial counterparty |
| Are you representing an association? |  |
| Country/Region | Europe |

**Introduction**

***Please make your introductory comments below, if any***

<ESMA\_COMMENT\_CD\_00>

The Commodity Markets Council Europe (CMCE) welcomes the opportunity to respond to the ESMA public consultation on technical standards for commodity derivatives. CMCE is highly supportive of efforts to enhance the functioning of EU commodity derivatives markets by optimising the applicable regulatory framework. Accordingly, we commend the European Commission and ESMA for their efforts to introduce targeted reforms to MiFID II/MiFIR through the Capital Markets Recovery Package (CMRP).

The reforms to the Ancillary Activity Exemption and the position limits regime reflect a pragmatic and flexible approach on the part of EU policymakers. Once fully implemented, the new regime will allow EU commodity markets to become nimbler and more conducive to the growth of new and nascent commodity markets. The changes introduced are positive in a number of regards in that they represent an adaptation to the post-Brexit reality and nature of the EU market, alleviate regulatory burdens on market participants and enable the growth of new commodity market segments essential to the transition to a more sustainable economy.

Accordingly, CMCE is pleased to contribute to this consultation process by providing substantive feedback on the proposals contained in the draft technical standards prepared by ESMA. CMCE is broadly favourable to many of ESMA’s proposals. However, in a limited number of cases, we have concerns over the necessity and potential efficacy of the suggested approach – notably in relation to spread contracts, EEOTC position reporting, and position management controls.

<ESMA\_COMMENT\_CD\_00>

**Questions**

1. : Do you agree with ESMA’s proposal regarding the impact of the new hedging exemption on the aggregation of positions? If not, please elaborate.

<ESMA\_QUESTION\_CD\_01>

CMCE agrees with ESMA’s proposal.

<ESMA\_QUESTION\_CD\_01>

1. : Do you agree with ESMA’s proposal for positions qualifying as risk-reducing? If not, please elaborate and provide an alternative proposal.

<ESMA\_QUESTION\_CD\_02>

CMCE agrees with ESMA’s proposal.

<ESMA\_QUESTION\_CD\_02>

1. : Do you agree with ESMA’s proposal on the application procedure for financial entities?? If not, please elaborate and provide an alternative proposal.

<ESMA\_QUESTION\_CD\_03>

CMCE agrees with ESMA’s proposal.

<ESMA\_QUESTION\_CD\_03>

1. : Do you agree with ESMA’s proposal on the application procedure for mandatory liquidity provision exemption? If not, please elaborate and provide an alternative proposal.

<ESMA\_QUESTION\_CD\_04>

CMCE agrees with ESMA’s proposal.

<ESMA\_QUESTION\_CD\_04>

1. : Do you agree with ESMA’s proposal on qualifying positions? If not, please elaborate and provide an alternative proposal.

<ESMA\_QUESTION\_CD\_05>

CMCE agrees with ESMA’s proposal.

<ESMA\_QUESTION\_CD\_05>

1. : Do you agree with ESMA’s proposed definition of financial entities? If not, please elaborate.

<ESMA\_QUESTION\_CD\_06>

CMCE agrees with ESMA’s proposal.

<ESMA\_QUESTION\_CD\_06>

1. : Do you agree with ESMA’s proposal regarding the aggregation and netting of positions in a commodity derivative? If not, please elaborate and provide an alternative proposal where available.

<ESMA\_QUESTION\_CD\_07>

CMCE agrees in principle with ESMA’s proposals with regard to the deletion of the reference to ‘the same commodity derivative’ to simplify the calculation of position limits for commodity derivatives that may be traded on trading venues in more than one jurisdiction. We note, however, that the draft language in article 3(1)(a) and (b) of draft RTS21a uses the formulation “….based on the same underlying and sharing the same characteristics traded … on other venues…”. The Level 1 governing provision (article 57(6) of MiFID2) clearly limits this to “other *trading* venues” rather than to “other venues”. For the avoidance of confusion, it would be better to reflect the Level 1 language more closely here.

CMCE also agrees in principle with the approach to aggregating ‘minis’ and ‘balmos’ transactions in the interest of simplicity. We note however that the reference to “balmos”/”minis” in article 3(2) of draft RTS21a should be limited to “commodity derivatives *traded on a trading venue* , that are a fraction of the value etc.”. As currently drafted, it would appear to catch OTC contracts, which is clearly not the intention described in the CP.

However, CMCE does not consider it necessary to include a reference to spread contracts. According to the experience of CMCE Members, the existing rules operate in such a way as to capture the constituent derivative contracts that form the basis of the spread contract. As a result, applying position limits to spread contracts would appear to be unnecessary and challenging given their heterogenous characteristics. Spread contracts are not listed as separate contracts but rather as a facility to enter into two legs in the outright contracts executed at the same time. The contracts that form the two legs are already subject to position limits. Including a reference to spread contracts is, therefore, unnecessary, adds a duplicative position limit and would give rise to an additional layer of complexity. CMCE does not see any regulatory benefit from this proposal, as the positions in the outright contracts would already be protected.

CMCE also notes that in the event a trading venue admits to trading a differential contract whose contract terms reflect the economics of two separate outright markets (for example a cash settled contract which reflects the difference between two separate outright contracts), a separate position limit is also not required. Instead, the position in the differential contract can be deconstructed into equivalent long and short positions and aggregated with any positions of the respective outright markets reflecting the economics of the differential.

Consequently, CMCE recommends that ESMA should remove the reference to spread contracts.

<ESMA\_QUESTION\_CD\_07>

1. : Do you agree with ESMA’s proposal for significant volumes? If not, please elaborate.

<ESMA\_QUESTION\_CD\_08>

CMCE agrees with ESMA’s proposal.

<ESMA\_QUESTION\_CD\_08>

1. : Do you agree with ESMA’s proposal? If not, please elaborate and provide an alternative proposal where available.

<ESMA\_QUESTION\_CD\_09>

CMCE has concerns about ESMA’s proposal, which it considers to be unnecessary, and believes it could have unintended adverse consequences.

ESMA’s proposal is that where “deliverable supply is substantially higher than total open interest”, NCAs would set the baseline figure for a spot month limit at 20% of the open interest and not by reference to deliverable supply. ESMA’s rationale for this is that in these circumstances *“the spot month limit is therefore deprived of any material effect, in contrast to the objectives of position limits set out in Article 57(1) of MiFID2”.* Recital 127 of MiFID2 explains those objectives as being *“…in order to prevent market abuse, including cornering the market, and to support orderly pricing and settlement conditions including the prevention of market distorting positions. Such limits should promote integrity of the market for the derivative and the underlying commodity without prejudice to price discovery on the market for the underlying commodity …”.*

Limits protect market integrity in spot month contracts by reducing the potential for the contract to become subject to an abusive squeeze (cornering). This risk materialises where there is sufficient constraint in the deliverable supply for there to be a real risk that participants wishing to make delivery would not be able to do so (commercially) at month end.

That risk does **not arise** in circumstances where the deliverable supply is substantially higher than the open interest. In those circumstances, not only would there be no risk of the market being cornered. In any event – clearly – imposing a limit on open interest (rather than on the deliverable supply) would not guard against any cornering risk. It would be a limit for the sake of a limit. This means that open interest is not the appropriate proxy to set a position limit.

It would potentially have some unintended consequences, reducing or placing a cap on liquidity in the spot month contract, which might impair the pricing of that contract and reduce the hedging benefit it presents to the market.

CMCE is not aware of any similar requirement under the rules of any other jurisdiction in respect to spot month contracts.

CMCE, therefore, requests ESMA to reconsider this proposal.

<ESMA\_QUESTION\_CD\_09>

1. : Do you agree with ESMA’s proposal? If not, please elaborate.

<ESMA\_QUESTION\_CD\_10>

It is the CMCE aim to ensure that the methodology works for all asset classes. Therefore, the CMCE would suggest the same approach as the one proposed to determine the open interest figure in Article 14 of draft RTS 21a. It establishes that the NCA calculates deliverable supply "over a representative period of time" which would depend on the characteristics of the commodity derivative. In our view, this would allow for an appropriate approach to be found for all asset classes.

CMCE believes that the approach adopted should be sufficiently flexible to ensure that the default measure used as a proxy does not turn out to be materially unrepresentative. Supply figures vary year-on-year in all commodity asset classes, and – to take an obvious example – the deliverable supply of wheat in a drought year would be a misleading measure to use for a good weather year. We therefore recommend that any such process should incorporate sufficient flexibility to allow for an exercise of judgement, on the basis of input from the relevant trading venues.

<ESMA\_QUESTION\_CD\_10>

1. : Do you agree with ESMA’s proposals regarding Article 14 of RTS 21a? If not, please elaborate and provide alternative proposals.

<ESMA\_QUESTION\_CD\_11>

CMCE agrees with the majority of ESMA’s proposals in relation to the calculation of open interest, as set out in Article 14 of the draft RTS 21a. Since the practice applied by NCAs has been subject to variation it is worth clarifying that open interest is to be calculated on a net rather than gross basis, consistent with the provisions of the Level 1 text.

It is also important to ensure that NCAs use comparable data sources to guarantee that open interest is calculated consistently. Accordingly, we agree that position reporting data provides a sound basis for the determination of open interest.

That said, in order for position reporting data to be established as a reliable, CMCE believes that ESMA and NCAs will have to increase their efforts to verify the accuracy of position reports – particularly when related to EEOTC contracts.

While CMCE understands ESMA’s proposed approach to calculating open interest by accounting for both trading activity on trading venues and in EEOTC contracts, we have doubts as to the practicability of this proposal. EEOTC contracts should only be included in the calculation of open interest once ESMA or NCAs have verified whether the contract genuinely qualifies as EEOTC.

CMCE notes that ESMA’s policy intention has always been to ensure that EEOTC are defined in a narrow manner, so as to limit the scope for firms to seek to avoid the impact of position limits unduly. This being so, it would be important for ESMA to ensure that a regime which includes EEOTC position reports should only include such reports when properly made. Otherwise, over time, if ESMA includes unfiltered EEOTC position reporting data in its open interest assessments, this will inevitably create the conditions for EEOTC to become accepted as a wider category.

CMCE notes that it is essential to align the EU regulatory efforts with other jurisdictions to ensure an internationally consistent framework which would work for globally active stakeholders, and which would ultimately benefit the European economy.

<ESMA\_QUESTION\_CD\_11>

1. : Do you see merit in the new approach considered by ESMA for new and less liquid agricultural commodity derivatives? If not, please elaborate and provide an alternative proposal.

<ESMA\_QUESTION\_CD\_12>

CMCE supports the changes to RTS 21 proposed by ESMA which would effectively impose a limit of 10.000 lots on all new and less liquid agricultural commodity derivative contracts below 20 000 lots (50 percent of the baseline). Contracts currently classed as ‘illiquid’ under the position limits framework receive a standardized limit of 2.500 lots and thereby effectively get a highly restrictive limit (resembling a baseline limit of 25 percent of open interest) when open interest increases close to 10.000 lots.

And whilst in theory, in line with ESMA Q&A’s on ‘commodity derivative topics’, NCA’s can use different derogations for illiquid markets which have an open interest between 5.000 and 10.000 lots, these remain difficult to apply in practice and are often not sufficient to mitigate the negative impact of disproportionately low position limits. Once the limit is reached, participants withdraw from the market, often switching to another trading venue outside of the MiFID II regime, thereby leaving the regulator no time to adjust the limit upwards.

<ESMA\_QUESTION\_CD\_12>

1. : Do you agree with ESMA’s proposal regarding Article 19 of RTS 21a? If not, please elaborate.

<ESMA\_QUESTION\_CD\_13>

CMCE is supportive of clarifying in Art. 19 par. 3, that where the open interest is significantly lower compared to the deliverable supply, NCAs shall adjust the other months’ position limit upwards to avoid the risk of unduly constraining trading.

However, the CMCE Members disagree with the need to adjust the spot month position limit downwards when open interest is relatively low compared to deliverable supply. In line with our answer to Q9 that, we do not see an increased risk of market manipulation in these situations. New contracts will always have a relatively low amount of open interest in their initial stages of development. There is no evidence to suggest that a more restrictive position limit provides any benefit to ensuring the orderly functioning of the market when there are no clear limitations in deliverable supply capacity. The CMCE Members are concerned that, if adopted, the ESMA proposal would hamper the development of such illiquid markets, without providing any benefit.

<ESMA\_QUESTION\_CD\_13>

1. : Do you agree with ESMA’ proposal regarding the upward adjustment factor to be used in case of a small number of market participants or less than three investment firms acting as market makers? If not, please elaborate and provide an alternative proposal.

<ESMA\_QUESTION\_CD\_14>

CMCE supports ESMA’s proposal to adjust the position limit upwards where there are less than ten market participants or where the commodity derivative is an agricultural commodity derivative with a net open interest below 300,000 lots and there are less than three investment firms acting market makers in that agricultural commodity derivative.

<ESMA\_QUESTION\_CD\_14>

1. : Do you agree with ESMA’s proposed amendments to ITS 4? If not, please elaborate.

<ESMA\_QUESTION\_CD\_15>

CMCE agrees with the proposal to delete securitized derivatives, and believes that also the rest of the amendments will improve the regime set by the ITS 4.

<ESMA\_QUESTION\_CD\_15>

1. : Do you agree with ESMA’s suggestion to introduce such ongoing position monitoring requirement in the draft RTS? If not, please elaborate.

<ESMA\_QUESTION\_CD\_16>

CMCE acknowledges that the revised scope of the position limits regime necessitates a more consistent, harmonised approach to position management requirements at the level of trading venues. As ESMA notes in Paragraph 108 of the consultation paper, trading venues are already required to ensure fair and orderly trading and maintain position management controls that reflect the specific risks associated with commodity derivatives trading on their platforms. The primary role of trading venues has contributed to meaningful and pragmatic position management controls with notable trading venues even establishing position controls below the limits mandated by regulation, as alluded to by ESMA.

In principle, CMCE agrees that, where appropriate and justifiable, a requirement to conduct ongoing position monitoring could be introduced. However, it is imperative that trading venues be granted discretion to initiate more regular periodic monitoring or ‘ongoing’ monitoring of positions held by market participants active on their platform only in specific cases where such monitoring would be warranted. We would strongly caution ESMA against adopting a prescriptive, ‘one-size-fits-all’ approach when devising requirements for position management controls given the heterogeneity among trading venues and market participants active in commodity markets.

This response should be read in conjunction with the CMCE answer to Question 17.

<ESMA\_QUESTION\_CD\_16>

1. : Do you agree with ESMA’s suggestion to introduce accountability levels as part of position management controls? Do you agree with ESMA’s assessment that accountability levels would be of particular relevance for physically settled commodity derivatives? If not, please elaborate and provide alternative proposals.

<ESMA\_QUESTION\_CD\_17>

As noted by ESMA in the consultation paper, the practice of establishing accountability levels is well established among trading venues. The accountability levels are set by individual trading venues and tailored to the specific conditions of their platform and the wider market for the related instruments

Accountability levels, if set as per the ESMA proposal, would require a far more regular exchange of information on positions than is necessary to protect market integrity. The regime could quickly become excessively burdensome and bureaucratic for both market participants and trading venues. Firms and trading venues would incur significant costs in terms of time, energy and effort without contributing in a meaningful sense to the preservation of orderly trading in commodity derivatives markets.

CMCE believes that it is essential for trading venues to be able to establish and adapt their own methodologies when establishing accountability levels. The venues should have full discretion in identifying the markets and periods to which the measures should apply. The venues should also have the discretion to establish whether further investigations and information requests are appropriate when an accountability level is breached. Ultimately, individual trading venues are most familiar with trading dynamics on their platform, the behaviour of market participants and the intricacies of the market, and thus best situated to devise the most appropriate methodology.

CMCE therefore recommends that trading venues retain the necessary discretion (i) in setting accountability levels for appropriate products, and (ii) as to whether to take any action (and if so, what) when a level is exceeded.   This would require the word “shall” to be replaced by “may” in Article 2 paragraphs 1, 2, 3 and the second part of paragraph 4.

For the sake of completeness, the CMCE notes that providing the trading venues with the discretion to set the accountability levels as they deem it necessary and appropriate would be in line with the CFTC rulemaking on position management controls, as well as with MiFID II Art. 57 par. 8, which lays down the powers for trading venues to establish position management controls. Accordingly, as a general comment, we would strongly advise ESMA against prescribing a common methodology or approach to setting accountability levels in future.

Further, we note that ESMA’s proposal would require trading venues to set accountability levels on positions held by firms and their “close links”. We would ask ESMA to consider this element carefully. It is not entirely clear how “close links” are intended to be defined, but it will be important to ensure that it does not give rise to breach of confidentiality or insider dealing risks for market participants. Participants in commodity derivatives markets often enter into joint ventures (JV) with non-group companies, subject to confidentiality restrictions and often have to impose information barriers between their trading functions and those trading on behalf the JV. In those cases, it would neither be possible nor legal for firms (a) to obtain information as to their JV partner’s trading position or (b) to manage their own position by reference to that information.

CMCE therefore recommends the deletion of the ‘persons with close links’ requirement throughout the new ESMA draft RTS on position management controls.

<ESMA\_QUESTION\_CD\_17>

1. : In your view, how should accountability levels be set for the spot month and the other months? Based on which methodology or criteria? Should all types of positions count towards the accountability levels?

<ESMA\_QUESTION\_CD\_18>

In view of the heterogeneity of trading venues and market conditions, CMCE believes that trading venues should be granted discretion to determine the optimal approach to the accountability levels introduced on their platforms. Trading venues should also be able to react promptly to market dynamics and adapt their accountability levels where appropriate.

<ESMA\_QUESTION\_CD\_18>

1. : Do you agree with ESMA’s suggestion to introduce requirements for the review of accountability levels? Do you also agree with ESMA’s proposal regarding reporting requirements to the NCA on accountability levels? If not, please elaborate.

<ESMA\_QUESTION\_CD\_19>

CMCE believes that trading venues can be relied upon to regularly review the appropriateness of the accountability levels that they apply. Introducing a requirement to report the methodologies they employ or any changes to accountability levels would be onerous if conducted on a ‘regular basis’.

In addition, CMCE does not believe that reporting on the application of accountability levels in practice through annual reports would enhance supervision.

<ESMA\_QUESTION\_CD\_19>

1. : In your view, what other types of position management controls could be further specified in the draft RTS?

<ESMA\_QUESTION\_CD\_20>

CMCE has no further suggestions for position management controls that would need to be further specified in the draft RTS.

<ESMA\_QUESTION\_CD\_20>

**Cost Benefit Analysis**

**CBA Q1**: This first question aims at identifying the category of firm/entity you belong to. Please provide the total notional amount traded in commodity derivatives traded on a trading venue (and EEOTC contracts where relevant in 2020 in thousand euros and the related total number of trades in the relevant boxes).

<ESMA\_QUESTION\_CD\_21>

TYPE YOUR TEXT HERE

|  |  |  |  |
| --- | --- | --- | --- |
| Category | Number of employees | Total notional amount traded in 2020 in thousand euros | Number of trades in 2020 |
| Trading venue | [1-50] |  |  |
| [51-250] |  |  |
| [251-500] |  |  |
| >500 |  |  |
| Financial entity | [1-50] |  |  |
| [51-250] |  |  |
| [251-500] |  |  |
| >500 |  |  |
| Non-financial entity | [1-50] |  |  |
| [51-250] |  |  |
| [251-500] |  |  |
| >500 |  |  |

<ESMA\_QUESTION\_CD\_21>

**CBA Q2**: for Financial entities: Do you intend to apply for an exemption for risk-reducing positions related to the commercial activities of the commercial entity of the group? What percentage of your positions do these risk-reducing positions account for?

<ESMA\_QUESTION\_CD\_22>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_CD\_22>

**CBA Q3**: Do you intend to apply for an exemption for positions resulting from transactions undertaken to fulfil mandatory liquidity provision? What percentage of your positions do these positions account for?

<ESMA\_QUESTION\_CD\_23>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_CD\_23>

**CBA Q4**: Is there any specific provision in draft RTS 21a that you would expect to be a source of significant cost? If so, please elaborate.

<ESMA\_QUESTION\_CD\_24>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_CD\_24>

**CBA Q5**: Taking into account the size of your firm, would you qualify overall compliance costs with draft RTS 21a as low, medium or high?

<ESMA\_QUESTION\_CD\_25>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_CD\_25>

**CBA Q6**: Is there any specific provision in the draft RTS on position management controls that you would expect to be a source of significant cost? If so, please elaborate.

<ESMA\_QUESTION\_CD\_26>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_CD\_26>

**CBA Q7**: Taking into account the size of your firm, would you qualify overall compliance costs with amended the draft RTS on position management controls as low, medium or high?

<ESMA\_QUESTION\_CD\_27>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_CD\_27>