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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 | ICE Endex |
| Activity | Regulated markets/Exchanges/Trading Systems |
| Are you representing an association? |  |
| Country/Region | Netherlands |

**Introduction**

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

<ESMA\_COMMENT\_CD\_00>

Intercontinental Exchange, Inc. (“ICE”) is a provider of marketplace infrastructure, data services and technology solutions to a broad range of customers including financial institutions, corporations and government entities. As an operator of regulated exchanges and clearing houses in major market centers around the world for a broad array of derivatives contracts and financial securities, ICE enables its customers to manage risk and raise capital. ICE's regulated exchanges include futures exchanges in the U.S., the U.K., the E.U., Singapore and (as of 2021) Abu Dhabi.

ICE Endex (“NDEX”), ICE's exchange based in continental Europe, provides liquid European gas, emissions and power markets that enable energy firms, EU ETS compliance entities and financial participants to effectively manage price risk. NDEX welcomes the opportunity to respond to the ESMA consultation paper on “technical standards for commodity derivatives - MiFID II recovery package”, which includes suggested changes to the technical standards for position limits (RTS 21), the position reporting framework (ITS 4) and proposes a new draft RTS for position management controls.

NDEX has always supported position management controls whereby a substantial responsibility for position monitoring, management and control is delegated to exchanges. Trading venues are best placed to conduct these tasks as position management regimes need to be cautiously calibrated and tailored to the circumstances of each individual exchange such as the nature of its membership and the characteristics of the underlying markets of contracts it admits to trading. There is no ‘one size fits all’ position management regime.

The recent amendments to the commodities derivatives section of MiFID II, as agreed by the co-legislators as part of the ‘COVID-19 pandemic recovery package’, sanctions this approach by granting exchanges additional powers to, amongst others, obtain information from market participants, rather than being prescriptive in the design of position management controls.

These powers can be used by an exchange as part of its position management controls in the context of an exchange’s broader market surveillance responsibility to facilitate fair and orderly markets. The amendments to MiFID II also impose an obligation on ESMA to develop draft regulatory technical standards to specify the content of position management controls, thereby taking into account the characteristics of the trading venues concerned.

NDEX generally agrees with ESMA’s proposal to introduce an ongoing position monitoring obligation and accountability levels as part of an exchange’s position management controls, but suggests two main areas for improvement of the draft RTS in order for the requirements to become workable in practice and prevent any possible unwanted consequences. Specifically, NDEX suggests amendments to ESMA’s proposals as regards the (1) widened scope of the position management arrangements; and (2) the level of prescriptiveness in the design of the controls. Lastly, NDEX warns against the possible introduction of further ESMA guidance in this area.

**Widened scope (‘persons with close links’)**

Article 58, paragraph 8 (a) of MiFID provides the power to exchanges to “monitor the open interest of persons”. The new ESMA draft RTS on position management controls expands the scope of this level 1 arrangement by adding “persons with close links”, which effectively introduces a wider obligation whereby exchanges must also consider open interest held by for example affiliates.

NDEX fundamentally does not see any legal basis for ESMA to expand the scope of the position management controls, as the level 1 mandate provided to ESMA was limited to the detailing of the content of the position management controls. The widening of the scope of the position management controls is not consistent with the agreement of the co-legislators. ESMA’s proposed widened scope would also introduce a foreign concept in the commodity derivatives section of MiFID II, distorting the consistency between the various components of the requirements applicable to commodity derivatives markets, including the position limits regime, position reporting requirements and the position management controls.

**Prescriptiveness in design of controls**

In Article 2 (1) of the new draft RTS on position management controls, ESMA introduces the obligation for trading venues to set accountability levels on physically settled commodity derivatives contracts. In the following paragraph (Article 2(2)), ESMA requires venues to request additional information from persons as to the nature and purpose of the position each time an accountability level is breached. Article 2(3) of the draft RTS also requires a trading venue to exercise its power to request a substantial amount of 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) with every breach of an accountability level.

The above detailed, highly-prescriptive process for the implementation of position management controls leaves little room for discretion, whilst market surveillance activities are apart from automated surveillance processes and alerts, an intuitive practice largely based on an exchange’s knowledge about underlying (physical) markets and its customers and products. For example, it may be appropriate for a firm to breach accountability levels on a frequent basis as the firm in question has a naturally large position in a given market. Mandatory information requests and investigations each time a breach occurs could considerably burden a market surveillance department which would distract from its core function.

The proposed requirements for the MiFID position management controls could necessitate considerable modifications to existing work processes and we note that attempts to increase harmonization at a granular level across markets has invariably resulted in unhelpful outcomes that must subsequently be resolved/refined. ICE therefore recommends introducing the necessary discretion for the exchange to set accountability levels for appropriate products and to allow discretion in the form of and need to take action towards market participants when breaches occur.

**Potential ESMA guidance**

In paragraph 120. (page 32.) of the consultation paper, ESMA states that it is minded to keep an open approach to the methodology to be used by trading venues to set accountability levels. However, in the same paragraph ESMA notes that there may be value in developing further guidance on the methodology, as this would contribute to a harmonized approach and level playing field across trading venues.

NDEX does not believe that any further detailing of the design of position management controls beyond what has already been put forward in the new draft RTS would be in line with the intent of the co-legislators. A harmonized methodology for setting accountability levels by means of ESMA guidance is unlikely to provide for sufficient granularity to be suitable for the broad variety of products exchanges offer for trading and risks imposing ill-calibrated controls with possibly highly undesirable outcomes. Ill-calibrated accountability levels could trigger frequent unnecessary alerts, burdening market surveillance and compliance staff with numerous information requests and investigations, distracting them from their core function of safeguarding fair and orderly markets.

Moreover, NDEX is firmly of the view that exchanges do not compete by lowering standards for market surveillance practices or could obtain any competitive advantage by not implementing an adequate methodology for setting accountability levels. On the contrary, it is essential to the business-interests of exchanges to run fair and orderly markets that can be trusted by their customers.

<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>

NDEX agrees with ESMA’s proposal and considers it to be in line with the intent of the co-legislators. Replicating the arrangements for qualifying positions for the hedging exemption currently in place for NFEs ensures consistency between the various exemptions and allows them to be used by financial entities in a non-discriminatory manner.

<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>

Yes, NDEX believes that it is appropriate to have an identical approach for classifying transactions as risk reducing for all positions held by financial entities and NFEs that qualify for a hedging exemption under the MiFID II position limits regime.

<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>

NDEX agrees with ESMA that the application procedure for NFEs should be copied for financial entities where possible. An identical application procedure provides for the equal treatment of the various market participants when applying for a hedging exemption and there are no apparent reasons for any differentiation.

<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>

Yes, NDEX supports the suggested procedure for the application procedure for the mandatory liquidity provision exemption.

<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>

Yes, NDEX supports the ESMA proposal on qualifying positions.

<ESMA\_QUESTION\_CD\_05>

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

<ESMA\_QUESTION\_CD\_06>

Yes, NDEX agrees with the proposed definition of financial entities.

<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>

Paragraph 2 of Article 3 of RTS 21a requires the positions of disaggregated components of a spread contract to be aggregated for the purpose of determining the position of a person in a commodity derivative. ICE notes that in its answer to question 10 of its Q&A on MiFID and MiFIR commodity derivative topics, ESMA rightfully recognises the difference between a spread trading strategy and a spread contract.

When spread trading is merely a trading strategy, whereby a market participant separately trades the two constituent legs of a spread, each consisting of outright futures contracts, no separate position limit is required. Positions resulting from a spread trading strategy will automatically result in positions in the outright futures that may be subject to the position limits regime.

NDEX 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.

NDEX furthermore agrees with the proposal to aggregate the positions of commodity derivatives that are based on the same underlying and share almost the same specifications as the principal or main commodity derivative traded on the same trading venue, such as "minis" and balance of month ("balmos"). NDEX notes that in ICE’s trading system a balmo can be either a trading strategy which for example in TTF gas covers a collection of daily futures contracts of two or more gas days from two business days ahead to the end of the contract month, or an outright futures contract.

<ESMA\_QUESTION\_CD\_07>

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

<ESMA\_QUESTION\_CD\_08>

Yes, NDEX agrees with the ESMA proposal for a definition for significant volumes.

<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>

NDEX disagrees with the proposal to set out in RTS 21a that, where the deliverable supply is significantly higher than the open interest, National Competent Authorities (“NCAs”) should set the baseline for the spot month limit as 25% of the open interest. NDEX fundamentally believes it is wrong to make use of the metric of open interest to calculate the position limit applicable to the spot month. Possible undesired behavior by market participants, in terms of market squeezing or cornering, can only occur when the delivery of a commodity is constrained in some form, i.e. deliverable supply is relatively low.

In this context, open interest is not a relevant metric for determining whether supply constraints exist and, therefore, its usage for determining the spot month limit could result in imposing an inappropriately set limit for the spot month. NDEX is especially concerned that the proposal could constrain the growth of new energy commodity derivatives at a stage of development when they would just become subject to the position limits regime, i.e. when open interest grows beyond 300.000 lots of open interest.

NDEX therefore strongly recommends the removal of the proposal to add to Article 11, paragraph 1: “Where the deliverable supply is substantially higher than the total open interest, competent authorities shall determine the baseline figure for the spot month limit by calculating 25% of the open interest in that commodity derivative.”

<ESMA\_QUESTION\_CD\_09>

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

<ESMA\_QUESTION\_CD\_10>

NDEX has no objections against the ESMA proposal to clarify in Article 12(2) of RTS 21a that the deliverable supply should be determined by reference to the average monthly amount of the underlying commodity available for delivery based on the most recent available data covering a one year period immediately preceding the determination. NCA’s however do need to maintain the existing flexibility to accommodate for markets where the number of expiries isn’t exactly twelve. It is for example common in agricultural contracts to have a more limited number of expiries over the course of a year. In this scenario the total annual deliverable supply should be divided by the number of expiries.

<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>

NDEX supports the ESMA proposal to calculate open interest on a net basis, based on position reporting data. NDEX furthermore strongly supports the proposal to calculate open interest "over a representative period of time" and notes that it may also be appropriate to calculate open interest on a forward-looking basis for contracts that experience a strong period of growth. NCA’s need a sufficient amount of flexibility to select an appropriate period of open interest to calculate a position limit, as the limit may otherwise have to be frequently adjusted or risks constraining the growth of a market.

<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>

NDEX 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>

NDEX does not believe it makes sense for NCAs to adjust the spot month position limit downwards when open interest is relatively low compared to deliverable supply. New contracts will always have a relatively low amount of open interest in their initial stages of development and 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.

<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>

NDEX 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>

NDEX believes the amendments will make a small improvement to 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>

As explained in more detail in our introductory comments, NDEX supports the general obligation on exchanges to monitor positions on an ongoing basis.

<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 explained in more detail in our introductory comments, NDEX believes it is important that exchanges have full discretion on the methodology for setting accountability levels, identifying the markets and periods to which they should apply and whether further investigations and information requests are appropriate when an accountability level is breached.

Apart from whether a contract is physically or financially settled, many more parameters are important in the assessment of whether an accountability level would be appropriate and meaningful for market surveillance purposes. Other parameters which are relevant for exchanges to consider include amongst others the amount of OTC trading vs on-exchange trading, liquidity established in the respective futures contract, whether there are any potential constraints in the delivery capacity (i.e. the relative size of the deliverable supply in the underlying of a futures contract) and whether a futures contract is price forming or its pricing is closely linked to another benchmark futures contract.

It is also important to provide sufficient flexibility for exchanges to apply accountability levels for the appropriate timeframe of a contract. As a market corner normally cannot occur more than a couple of days before the delivery of a contract, it may not be useful to set an accountability level for months ahead of delivery.

NDEX therefore recommends introducing the necessary discretion for the exchange to set accountability levels for appropriate products and to allow discretion in the form of and need to take action towards market participants when breaches occur. This approach would be best achieved by replacing the word “shall” with “may” in paragraph 1, 2 and 3 and the second part of paragraph 4 of Article 2 of Article 2 of 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>

As explained in more detail in our introductory comments, NDEX believes it is inappropriate to widen the scope of the position management regime to include ‘persons with close links’ and further detailing the methodology or criteria for setting accountability levels as part of the technical standards or subsequent ESMA guidance. NDEX therefore recommends the deletion of the ‘persons with close links’ requirement throughout the new ESMA draft RTS on position management controls.

<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>

To ensure accountability levels continue to be set at appropriate levels, NDEX supports the requirement to review accountability levels. NDEX has no objection to report breaches of accountability levels to its NCA.

<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>

NDEX 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>

Yes, NDEX believes that the absence of sufficient discretion for the exchange to implement the position management controls in an appropriate manner and the extension of the position management controls to cover ‘persons with close links’ is likely to result in a significant cost to the exchange and market participants.

Any breach of an accountability level would require the exchange to investigate and obtain a substantial amount of information from market participants. Exchanges may have to hire additional market surveillance staff to handle all investigations prompted by alerts and market participants may have to hire additional compliance staff to respond to all information requests.

The extension of the scope of the position management controls to cover ‘persons with close links’ would require new daily reporting arrangements between the exchange and their clients to be developed, as the information about affiliates covered under the ‘persons with close links’ requirement is not covered in existing MiFID II position reporting requirements.

<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>

NDEX would qualify the estimated compliance costs with the draft RTS on position management controls as unreasonably high and disproportionate.

<ESMA\_QUESTION\_CD\_27>