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MiFID II – Position Limits on Commodity Derivatives

Expert Group on agricultural commodity derivatives and spot markets,

9th November 2016

MiFID II

Goals:

- To prevent market abuse and
- support orderly pricing and settlement conditions.

Instrument:

Application of position limits to commodity derivatives and economically equivalent derivatives by Articles 57, 58 of Dir. 2014/65/EU (MiFID II). Regulatory Technical Standards in preparation.

RTS 21 is not yet adopted by the Commission therefore details can still be changed!

Time Schedule:

Implementation into national law, taking effect from 03.01.2018 on.

Commodity Derivatives

Commodity Derivatives are derivatives on

- commodities, energy, climatic variables etc. as underlyings,

in the form of Futures, Options, Swaps and Securitised derivatives

and

- Economically equivalent OTC-contracts.

Scope

- Position limits do apply to every natural person and corporate entity holding commodity derivatives within the EU. These are
  - positions held by that person in a particular commodity derivative traded on a trading venue (EEA regulated markets, MTFs and OTFs),
  - positions held by that person in the <u>same</u> commodity derivative traded on another trading venue and
  - Economically equivalent OTC contracts.
- Hence, position limits do also apply to third country counterparties who entered into contracts on EU venues or trade through investment firms seated in the EU.

Commodity Derivative

The commodity derivative to which the position limit applies is

- a type of contract,
  - i.e. all contracts with identical terms that can be netted
- that is traded on a trading venue

and

- economically equivalent OTC-contracts.

⇨ Non-economically-equivalent OTC-contracts are not covered.

Netting

The position limit applies to the net position which is

- the Balance of long and short positions of
- a person or at group level.

Hedge positions can be exempted.

Relevant Time Frame

As every contract is comprised of a series of contracts of different maturities we differentiate between:

- One Limit to the contract with the maturity next to expire („spot-month")
- A limit to any other contract that is not spot month contract („other months").

Relevant Underlying

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- Spot month limit is calculated by identifying deliverable supply (quantity of underlying that can be used to fulfil delivery requirements)
  - Specifications for different commodities still to be developed
- Other months limit is calculated by identifying open interest on trading venue (aggregated number of lots that are outstanding)

Hedge-Exemption

- Non financial entities can apply for an exemption of positions that are reducing risks directly relating to the commercial activity of that non financial entity.

  Netting is not possible anymore with exempted positions.

- Application to Central Competent Authority, i.e. authority of jurisdiction in which relevant trading venue is located. Details of requirements and application process will be dealt with by national legislator.

Calculating Position Limits

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- Definition of position limit:

Position limit is the highest long/short position a person may hold during the validity period of the position limit.

- NCA sets the limit once a year within a range of 5% - 35% of deliverable supply/open interest, depending on
  - Liquiditity, number of market participants, storage capacity etc.
- For agricultural contracts limit can be lowered to 2,5%!

Illiquid Markets

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Markets with a total combined open interest of spot and other months contracts not exceeding 10.000 lots limit is set at 2.500 lots.

Thus, if open interest is even below 2500 lots market participants can hold up to 100%.

Weekly Report

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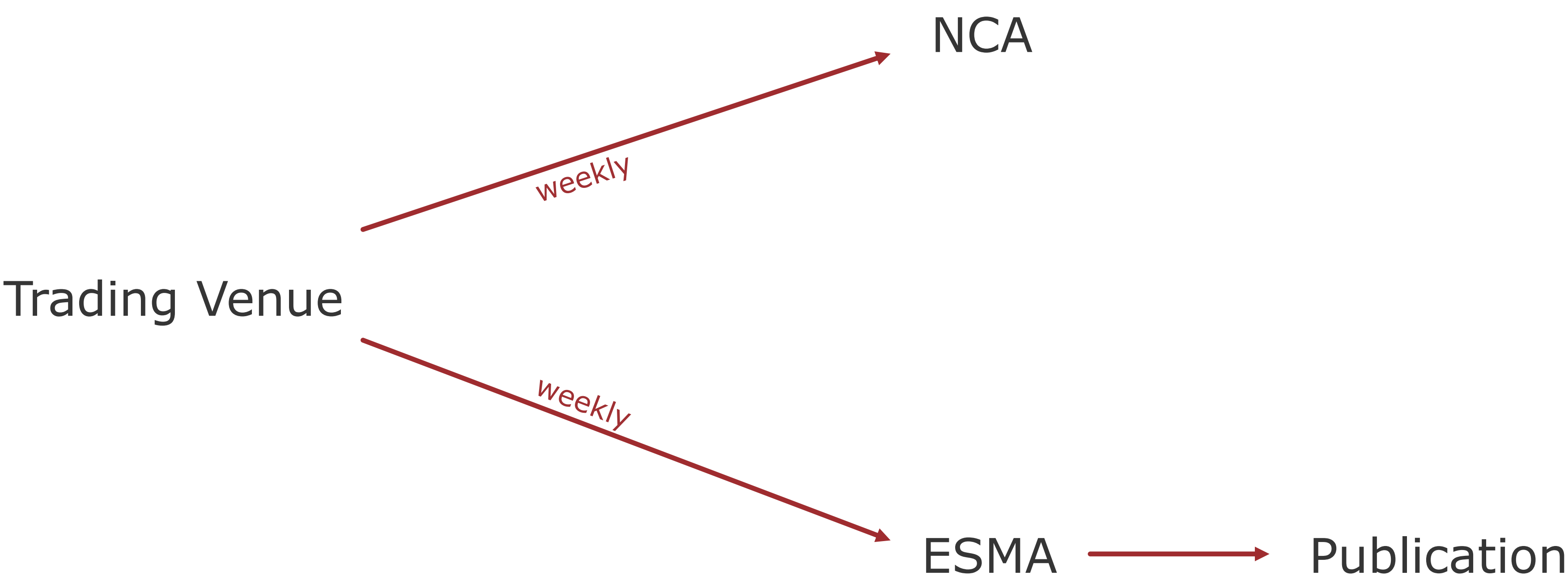

Daily Reporting at Trading Venues

End client $\xrightarrow{\text{daily}}$ Intermediary $\xrightarrow{\text{daily}}$ Broker $\xrightarrow{\text{daily}}$ Trading Venue $\xrightarrow{\text{daily}}$ NCA $\xleftrightarrow{\text{Exchange with CCA}}$ CCA

Daily Reporting OTC

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End client $\xrightarrow{\text{daily}}$ Financial Intermediary $\xrightarrow{\text{daily}}$ Investment firm $\xrightarrow{\text{daily}}$ NCA / CCA

Thank you for your attention!