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Committee on Industry, Research and Energy

2011/0298(COD)

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DRAFT OPINION

of the Committee on Industry, Research and Energy

for the Committee on Economic and Monetary Affairs

on the proposal for a directive of the European Parliament and of the Council on markets in financial instruments repealing Directive 2004/39/EC of the European Parliament and of the Council (recast)
(COM(2011)0656 – C7-0382/2011 – 2011/0298(COD))

Rapporteur: Holger Krahmer

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SHORT JUSTIFICATION

The Markets in Financial Instruments Directive (MiFID, 2004/39/EC), in force since November 2007, is one of the EU's cornerstones of financial regulation and your Rapporteur acknowledges the need of a revision of the current MiFID (hereinafter called MiFID II) in order to correct its weaknesses and provide for both an improved transparency and regulation of financial markets.

Exemptions under MiFID

Your Rapporteur finds that several exemptions of the scope in MiFID II proposal are misleading or not clear enough and tabled some amendments in order to clarify them.

In general your Rapporteur believes that non-financial firms like commodities industries should, due to their nature, not be fully covered by the MiFID. This approach is also fully in line with the Commissions intention explained in recital 88, that it should be ensured that activities by non-financial firms involving for example the hedging of production-related and other risks on an ancillary basis should be remain exempted. These trading activities of non-financial firms pose no systemic risk and are an essential element of the companies' business.

Other clarifications mainly refer to the criteria for defining whether an activity is ancillary to the main business. The main principles for this definition should not be left to delegated acts and this definition should include the fact that an activity can only be ancillary when it is a means of risk management for the main business, and when the size of the activity is considerably smaller than the main business.

If, under MiFID, non-financial firms are considered as financial firms, they have to fulfil costly obligations of several financial regulations. For example they become subject to the clearing obligation of all their standardised 'over-the-counter' derivate transactions as defined under the European Market Infrastructure Regulation (EMIR) or might be required to hold a capital buffer under the Capital Requirements Directive (CRD) after 2014.

As a result, both EMIR and CRD would stipulate companies to hold more capital as a reserve for their necessary trading activities, hampering the companies' ability to invest. Also risk management becomes much more expensive and as a consequence some companies, especially SMEs, would refrain from risk management or at least do so to a lesser extent.

Most SMEs can not afford to participate directly in traded markets themselves to manage the risks related to their main business and therefore they have set up joint entities to create a critical mass to access traded markets with the aim to manage risks of their main business. These company structures need also to be addressed, in order to guarantee appropriate exemptions for non-financial SMEs and their joint entities.

Classification of financial instruments

Physically settled forward products in MiFID II proposal are classified as financial instruments. However, these forwards are crucial for risk management of commercial firms and are fundamentally different from speculative financial instruments - they do not involve any financial (cash) settlement and the underlying physical commodity will actually be delivered on schedule. Consequently physically settled forwards do not pose any risk to financial markets. The consequences of physical forward products being considered financial instruments include several implications under MiFID, EMIR and the Market Abuse Regulation (MAR).

The current MiFID II proposal reduces the ability of firms to take advantage of the ancillary activity exemption (Article 2(1)(i)) as the majority of their trading is in physical forward contracts. Also physically settled forwards could then be subject to position limits outlined in Article 59. Under EMIR, the classification of physically settled forwards as financial instrument would increase the probability for non-financial firms to hold positions beyond the so-called clearing threshold which would make them subject to the clearing obligation. Furthermore, physically settled forwards will fall under the scope of MAR.

In comparison, the respective draft law in the United States (i.e. Dodd-Frank-Act) uses another definition of financial instruments which also excludes physically-settled derivatives expressively. Besides, physically settled forwards in the energy sector are already covered by the Regulation on wholesale energy market integrity and transparency (REMIT).

Your Rapporteur therefore proposes to explicitly exclude products that can be physically settled and that are entered into for commercial purposes and do not display the characteristics of other derivative financial instruments.

Position limits

Limiting firms' positions in the derivative market will constrain their ability to efficiently manage risks or access emission allowance markets which will ultimately increase costs and the overall risk level in their sector. Moreover, it may force them to seek hedging opportunities in other less liquid and riskier markets, pushing up risk management costs and ultimately prices to consumers. Your Rapporteur therefore prefers the position management approach as referred in MiFIR Article 35(1), because this is more flexible and better tailored for the characteristics of the market.

AMENDMENTS

The Committee on Industry, Research and Energy calls on the Committee on Economic and Monetary Affairs, as the committee responsible, to incorporate the following amendments in its report:

Amendment 1

Proposal for a directive
Recital 22 a (new)

Text proposed by the Commission	*Amendment*
	(22a) For a well-functioning internal market in electricity and natural gas, and for the carrying out of the Transmission System Operators' (TSOs) tasks under Directive 2009/72/EC, Directive 2009/73/EC, Regulation (EC) No 714/2009, Regulation (EC) No 715/2009, or network codes and guidelines adopted pursuant to those Regulations, it is necessary that TSOs and their service providers are exempted when issuing transmission rights, in the form of either Physical Transmission Rights or Financial Transmission Rights, and when providing a platform for secondary trading. In order to enable efficient trade in transmission rights it is further necessary to exempt any person when buying or selling those transmission rights.

Or. en

Justification

The qualification of Physical Transmission Rights (PTRs) and Financial Transmission Rights (FTRs) as financial instruments may well result in market players refraining from trading in transmission rights as they may consider the requirements under MiFID as too burdensome. However, trade in PTRS and FTRs, because of their risk hedging functions, is an important contribution to the efficient functioning of the internal energy market and should therefore be exempted from MiFID.

Amendment 2

Proposal for a directive
Recital 88

Text proposed by the Commission	*Amendment*
(88) Considering the communiqué of G20	(88) Considering the communiqué of G20

finance ministers and central bank governors of 15 April 2011 on ensuring that participants on commodity derivatives markets should be subject to appropriate regulation and supervision, the exemptions from Directive 2004/39/EC for various participants active in commodity derivative markets should be modified to ensure that activities by firms, which are not part of a financial group, involving the hedging of production-related and other risks as well as the provision of investment services in commodity or exotic derivatives on an ancillary basis to clients of the main business remain exempt***, but that firms*** specialising in trading commodities and commodity derivatives are brought within this Directive.	finance ministers and central bank governors of 15 April 2011 on ensuring that participants on commodity derivatives markets should be subject to appropriate regulation and supervision, the exemptions from Directive 2004/39/EC for various participants active in commodity derivative markets should be modified to ensure that activities by firms, which are not part of a financial group, involving the hedging of production-related and other risks as well as the provision of investment services in commodity or exotic derivatives on an ancillary basis to clients of the main business remain exempt***. It has to be kept in mind that firms whose main business is producing and/or supplying a commodity and which trade on own account in commodity derivatives as an ancillary activity are already subject to tailor-made regulatory oversight and to regulatory reporting obligations specifically to spot and physical forward transactions by virtue of Regulation 2011/1227/EC (REMIT) and are subject to regulatory reporting obligations in respect of standard derivative transactions and regulatory oversight by virtue of Regulation [ ] (EMIR). Firms*** specialising in trading commodities and commodity derivatives ***however should be*** brought within this Directive.

Or. en

Justification

Commercial firms already covered by EMIR and sector-specific regulation (i.e. REMIT, Regulation 2011/1227/EC) should remain exempted from MiFID, provided that this is an ancillary activity to their main business. REMIT includes an effective and appropriate market oversight framework and transaction reporting requirements explicitly covering transactions falling outside the MiFID scope. In addition to this, EMIR will also provide the framework providing transaction reporting and central clearing or other risk management obligations.

Amendment 3

Proposal for a directive
Article 2 – paragraph 1 – point d – subparagraph 2

Text proposed by the Commission	*Amendment*
This exemption does not ***apply to*** persons ***exempt under Article 2(1)(i)*** who deal on own account in financial instruments as members or participants of a regulated market or MTF, including as market makers in relation to commodity derivatives, emission allowances, or derivatives thereof;	This exemption does not ***prevent*** persons who deal on own account in financial instruments as members or participants of a regulated market or MTF, including as market makers in relation to commodity derivatives, emission allowances, or derivatives thereof***, to be exempted under another applicable exemption of this Article***;

Or. en

Justification

A clarification is needed to ensure that this exemption does not prevent persons exempted under Article 2(1)(i) from being exempted under another applicable rule included in Article 2.

Amendment 4

Proposal for a directive
Article 2 – paragraph 1 – point i – indent 3 a (new)

Text proposed by the Commission	*Amendment*
	- deal on own account in financial instruments by executing orders of their owners and their affiliates in case of jointly managed undertakings;

Or. en

Justification

The exemptions described in the Commission proposal do not pay due attention to characteristic company structures, in particular as regards SMEs. This amendment is intended to avoid discriminations towards SMEs that cannot afford to participate directly in traded markets and therefore set up a joint entity or engage in strategic agreements with third entities in order to create a critical mass to access traded markets to manage the risks related to their main business. Linked to Amendment 5.

Amendment 5

Proposal for a directive
Article 2 – paragraph 1 – point i – subparagraph 2

Text proposed by the Commission	*Amendment*
provided that in all cases this is an ancillary activity to their main business, when considered on a group basis, and that main business is not the provision of investment services within the meaning of this Directive or banking services under Directive 2006/48/EC;	provided that in all cases this is an ancillary activity to their main business when considered on a group basis ***or to the main business of the owners and their affiliates where the services are provided by jointly managed undertakings***, and that main business is not the provision of investment services within the meaning of this Directive or banking services under Directive 2006/48/EC;

Or. en

Justification

The exemptions described in the Commission proposal do not pay due attention to characteristic company structures, in particular as regards SMEs. This amendment is intended to avoid discriminations towards SMEs that cannot afford to participate directly in traded markets and therefore set up a joint entity or engage in strategic agreements with third entities in order to create a critical mass to access traded markets to manage the risks related to their main business. Linked to Amendment 4.

Amendment 6

Proposal for a directive
Article 2 – paragraph 1 – point k

Text proposed by the Commission	*Amendment*
(k) firms which provide investment services and/or perform investment activities consisting exclusively in dealing on own account on markets in financial futures or options or other derivatives and on cash markets for the sole purpose of hedging positions on derivatives markets or which deal for the accounts of other members of those markets or make prices for them and which are guaranteed by clearing members of the same markets,	(k) firms***:***

where responsibility for ensuring the performance of contracts entered into by such firms is assumed by clearing members of the same markets;

(i) which provide investment services and/or perform investment activities consisting exclusively in dealing on own account on markets in financial futures or options or other derivatives and on cash markets for the sole purpose of hedging positions on derivatives markets, or

(ii) which deal for the accounts of other members of those markets or make prices for them and which are guaranteed by clearing members of the same markets, where responsibility for ensuring the performance of contracts entered into by such firms is assumed by clearing members of the same markets;

Or. en

Justification

The text should be split into two different characteristics so that it is fully clear that firms can use the exemption either under point (k)(i) or point (k)(ii).

Amendment 7

Proposal for a directive
Article 2 – paragraph 1 – point n

Text proposed by the Commission	*Amendment*
(n) transmission system operators as defined in Article 2(4) of Directive 2009/72/EC or Article 2(4) of Directive 2009/73/EC when carrying out ***their*** tasks under those Directives or Regulation (EC) 714/2009 or Regulation (EC) 715/2009 or network codes or guidelines adopted pursuant those Regulations.	(n) transmission ***and distribution*** system operators as defined in Article 2(4) ***and (6)*** of Directive 2009/72/EC or Article 2(4) ***and(6)*** of Directive 2009/73/EC ***as well as storage and LNG system operators as defined in Article 2 (10) and (12) respectively of Directive 2009/73/EC and persons acting as their service providers*** when carrying out ***the system operators'*** tasks under those Directives or Regulation (EC) 714/2009 or Regulation (EC) 715/2009 or network codes or guidelines

adopted pursuant those Regulations, ***such as the issuance of transmission rights, or other capacity rights, and the provision of a platform for secondary trading, and any other persons when buying and/or selling such transmission rights or other capacity rights; this exemption applies only with regard to the aforementioned activities.***

Or. en

Justification

Transmission system operators (TSOs), distribution system operators (DSOs) and storage operators play a key role in the well functioning of the internal energy market, guaranteeing security of supply and offering access to transport, distribution or storage capacities in a competitive and fair way. Therefore the exemption regime should be extended to fully cover such infrastructure operators' activities.

Amendment 8

Proposal for a directive
Article 2 – paragraph 3 – subparagraph 2

Text proposed by the Commission	*Amendment*
The criteria for determining whether an activity is ancillary to the main business shall take into account at least the following elements:	The criteria for determining whether an activity is ancillary to the main business shall take into account at least the following elements:
- the extent to which the activity is objectively measurable as reducing risks directly related to the commercial activity or treasury financing activity,	***(a)*** the extent to which the activity is objectively measurable as reducing risks directly related to the commercial activity or treasury financing activity,
- the capital employed for carrying out the activity**.**	***(b)*** the capital employed for carrying out the activity ***or the risk stemming from the activity, both as a proportion to the activities of the group,***
	(c) the activity relates to the management of commodity risks or other risk arising from the commercial business of the group.

Or. en

Justification

In order to apply the principles referred to in recital 88, it is necessary to provide a clear exemption for activities by non-financial firms "involving the hedging of production-related and other risks". Besides point (a), the ancillary character needs to be justified by comparing the size of the activity (by means of capital or risk employed) to the size of the main business and it should be ensured that commercial firms are only dealing in financial instruments related to the main business of the group of companies to which the entity/person belongs.

Amendment 9

Proposal for a directive
Article 4 – paragraph 2 – point 25a (new)

Text proposed by the Commission	*Amendment*
	25a) 'Jointly managed undertaking' means a jointly managed undertaking within the meaning of Article 32 of Directive 83/349/EEC;

Or. en

Justification

Necessary to refer to Directive 83/349/EEC for applying the newly introduced exemption in Amendments 4 and 5.

Amendment 10

Proposal for a directive
Article 59 – paragraph 1a (new)

Text proposed by the Commission	*Amendment*
	1a. Commercial firms shall not be subject to position limits for those products that are used for risk management activities or which use results from regulatory compliance obligations.

Or. en

Justification

Limiting firms' positions in the derivative market will constrain their ability to efficiently manage risks or access emission allowance markets which will ultimately increase costs and the overall level of risk in their sector. It may also force them to seek hedging opportunities in

other less liquid and riskier markets. The position management approach as referred in MiFIR Article 35(1) is a better alternative.

Amendment 11

Proposal for a directive
Article 60 – paragraph 2

Text proposed by the Commission	*Amendment*
2. In order to enable the publication mentioned in point (a) of paragraph 1, Member States shall require members and participants of regulated markets, MTFs and OTFs to report to the respective trading venue the details of their positions ***in real-time,*** including any positions held on behalf of their clients.	2. In order to enable the publication mentioned in point (a) of paragraph 1, Member States shall require members and participants of regulated markets, MTFs and OTFs to report to the respective trading venue the details of their positions ***on a weekly basis***, including any positions held on behalf of their clients.

Or. en

Justification

Reporting requirements have to be proportionate for non-financial firms. Platforms do not need real time information to be able to provide weekly position reports. Real-time reporting would be extremely costly and burdensome for non-financial firms.

Amendment 12

Proposal for a directive
Annex I – section C – point 6

Text proposed by the Commission	*Amendment*
(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, an OTF, and/or an MTF;	(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, an OTF and/or an MTF ***and are not entered into for commercial purposes and display the characteristics of other derivative financial instruments***;

Or. en

Justification

Physically settled forward products are essential for commercial firms. The consequences for considering them as financial instruments are not proportionate for non-financial firms and include negative implications regarding:

- *reduced possibility to use the ancillary activity exemption mentioned in Article 2(1)i;*
- *Market Abuse Regulation compliance;*
- *increased probability for non-financial firms to hold positions beyond the clearing threshold under EMIR and become subject to the clearing obligation;*
- *physical forward contracts would become subject to position limits.*