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COMMISSION DELEGATED REGULATION (EU) …/...

of 1.12.2016

supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the criteria to establish when an activity is considered to be ancillary to the main business

(Text with EEA relevance)

1. CONTEXT OF THE DELEGATED ACT

The Markets in Financial Instruments Directive (Directive 2014/65/EU, MiFID II) exempts persons dealing on own account, or providing investment services to clients, in commodity derivatives, emission allowances or derivatives thereof, provided this is an ancillary activity to their main business on a group basis and the main business is not the provision of investment services within the meaning of MiFID II or banking activities under Directive 2013/36/EU.

In this context, Article 2(4) of MiFID II empowers the Commission to adopt regulatory technical standards (RTS) specifying the criteria for establishing when an activity is to be considered ancillary to the main business of a group.

The European Securities and Markets Authority (ESMA) submitted a draft RTS to the Commission on 28 September 2015. On 20 April 2016, the Commission notified ESMA, in accordance with Article 10(1) of Regulation No (EU) 1095/2010, of its intention to endorse this draft RTS subject to a number of changes. In order to ensure that the main business test is more indicative of the main business activities of a group, the Commission proposed that a capital based test be developed to distinguish a group's main activities from its ancillary activities. Groups which have undertaken significant capital investments, relative to their size, in the creation of infrastructure transportation and production facilities, as well groups that have undertaken investments which cannot be easily hedged in financial markets should be given an opportunity to avail themselves of the capital test because this test would be a more accurate reflection of their main activities. The Commission therefore asked ESMA to develop a methodology to allocate capital between the main business activity and the ancillary activity so as to allow groups to demonstrate, on the basis of capital employed, where the group's main business activity resides.

On 30 May 2016, ESMA submitted to the Commission a formal opinion and a revised draft technical standard. In its opinion ESMA did not propose a single capital based methodology but rather proposed a number of possible methodologies and metrics for calculating and allocating capital between a group's activities. In its 30 May opinion, ESMA set out five options for the numerator (denoting speculative trading) and three options for the denominator (denoting a group's main activity).

ESMA, in its opinion, did not indicate any preferences among the different options it presented to the Commission. ESMA also refrained from suggesting a threshold denoting the percentage of speculative trading in relation to a group's main activity that would trigger the need to obtain a licence under MiFID II.

With respect to the **numerator** (which denotes the capital employed for "speculative" trading activity) ESMA submitted five options. These options were assessed against the aims of creating a workable capital based test:

(1) *Option 1 - Gross notional value of derivatives trading*. This option has the benefit of simplicity and availability but, importantly, it is <u>not</u> a capital allocation measure. The use of "gross notional" is therefore not in line with the aim to establish a 'capital allocation' measure.

(2) *Option 2 - Simplified approach derived from the Capital Requirements Regulation* (*Regulation 575/2013, CRR)*. This option is relatively simple, although groups may need some initial guidance on how to apply it in practice.

Option 2 has the advantage of being a capital measure (capital is calculated as 15% of the net derivative position plus 3% of the gross derivative position).

(3) *Option 3 - Mark-to-market (MTM) valuation of speculative derivatives.* This is not a capital measure, but rather a measure reflecting the "risk profile" or "financial exposure" of a firm. The measure is also subject to considerable volatility as the value of both positive and negative exposures is in permanent flux, in line with underlying markets. Furthermore, the mark-to-market measure exposes groups and competent regulators to the risk that results are unreliable as they would be exposed to considerable price volatility, notably on short positions.

(4) *Option 4 - Approach based on margin requirements for exchange traded derivatives.* Apart from not being a capital measure, this measure also has the disadvantage of overestimating the speculative activity of a company by including margin posted for hedging positions. But this measure could also underestimate speculative trading of a firm that speculates in OTC derivatives, where no margin needs to be posted.

(5) *Option 5 - Approach based on the European Supervisory Authorities' methodology for margin requirements for OTC derivative contracts which are not centrally cleared*. While this measure could be easily adapted for the purposes of MIFID II, ESMA did not submit a calibration methodology in how to apply this test in practice.

Based on the above assessment, the most suitable measure to determine the size of non-hedging trading activities is the one based on the simplified CRR method. This is because this metric is derived from an internationally agreed framework for regulatory capital and it gives a proportionate measure of the size of the positions in commodity derivatives. It is directly related to the gross amount of trading, which represents the activity in this sector. Other measures identified by ESMA are less sophisticated capital metrics, or measure the profit (or loss) of the trading position rather than the activity itself. On careful consideration of the most accurate measure and the complexity of implementation of the capital based test, the CRR metric is the most attractive.

With respect to the **denominator** (which denotes the capital employed in the pursuit of a group's main business activity), the following options were assessed:

(1) Accounting measure of Plant Property and Equipment ('PP&E'), or

(2) Total equity, or

(3) Other measures of financing (combining debt and equity).

PP&E is not suitable for intermediaries with low investment in PP&E, whereas total equity fails to reflect all the investments in operational infrastructure when they are financed through debt. A broader measure of financing, such as capital employed, would avoid these shortcomings. Capital employed would be calculated as the group's total equity plus its long-term liabilities or, alternatively, total assets minus short-term liabilities of the group.

ESMA, in its opinion of 30 May, signalled that such a wider measure of financing may be appropriate. This option would closely resemble the generally accepted measure of "capital employed" by combining total equity with long term debt. This metric is the most suitable to measure the capital employed in a diversified group's main activity.

There is, however, a risk that a total equity plus debt measure may be prone to overestimating a group's main business activity, as equity and debt could also be used to finance noncommercial or speculative assets of a company. The capital employed measure, would therefore have to be applied in a prudent manner. On balance, this shortcoming can be overcome by sufficiently prudent regulation. Capital employed would, therefore, remain the most suitable measure denoting a group's main activity.

With respect to the **applicable threshold**, ESMA, in its draft RTS of 28 September, proposed a 10% threshold. As the capital test, like the trading test ESMA proposed in the draft of 28 September, aims at capping the amount of speculative derivatives trading a group may engage in without requiring authorisation under MiFID II, it appears appropriate to retain a threshold of 10% also in relation to the capital test.

In order to address the legal uncertainty that would arise for those non-financial groups that do not have a complete and representative set of data covering their main and ancillary activities, a calculation period of three years is introduced. If calculated annually, the amount of capital employed and the size of the trading activity in financial instruments might fluctuate from year to year as, for example, events that occur periodically may require increased hedging activities in certain years but not in others. Therefore, a non-financial group may fall within the scope of MiFID II because it fulfils the relevant criteria in one year; however, it may qualify for an exemption from MiFID II in another year. In order to address this practical issue of an "oscillator" group, the calculations to be undertaken to verify whether non-hedging trading is ancillary or not need should cover a rolling average of three years.

2. CONSULTATIONS PRIOR TO THE ADOPTION OF THE ACT

In accordance with Article 10 of the Regulation (EU) 1095/2010 ESMA has carried out a public consultation on the draft regulatory technical standards. A consultation paper was published on 19 December 2014 on the ESMA website and the consultation closed on 2 March 2015. In addition, the ESMA invited sought the views of the Securities and Markets Stakeholder Group (SMSG) established in accordance with Article 37 of the ESMA Regulation. The SMSG chose not to provide advice on these issues due to the technical nature of the standards.

Together with the draft technical standards, and in accordance with the third subparagraph of Article 10(1) of Regulation (EU) No 1095/2010, the ESMA has submitted its impact assessment, including the analysis of costs and benefits related to the draft technical standards. This analysis is available at https://www.esma.europa.eu/databases-library/esma-library

3. LEGAL ELEMENTS OF THE DELEGATED ACT

The right to adopt a delegated Regulation is provided for under Article 2(4) of MiFID II. Under these provisions, the Commission is empowered to adopt a delegated act to set out the conditions under which an activity is to be considered as ancillary to the main business by specifying three tests:

- Article 1 specifies the scope and aim of the delegated regulation which is to define the activities of a person that shall be deemed 'ancillary' to the main business of a group to which that person belongs.
- Article 2 contains a "market share test" with corresponding trading activity thresholds that compares the level of a person’s trading activity against the overall trading activity in the EU on an asset class basis.

- Article 3 contains a "main business test" with corresponding thresholds, to determine whether non-hedging trading in commodity derivatives constitutes a minority of activities at group level. The size of the main business activity can be calculated by aggregating the trading activity of a person in all of the asset classes referred to in Article 2 or by estimating the capital for the trading activity in commodity derivatives, emission allowances and derivatives thereof according to the method set out in the fifth paragraph of this Article.
- Article 4 sets out the precise details for calculating the size of a group's trading activities, the applicable reference periods as well as the date as of which the relevant trading or capital data needs to be collected. .
- Article 5 contains the criteria for differentiating between non-hedging transactions in derivatives and those transactions that can be considered as objectively measurable as reducing risk directly relating to commercial activity or treasury financing activity (hedging). Such hedging transactions do not count towards the trading activity to which the exemption applies as measured in the numerator in both tests.

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(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments[1], and in particular Article 2(4) thereof,

Whereas:

(1) The assessment whether persons are dealing on own account or are providing investment services in commodity derivatives, emission allowances and derivatives thereof in the Union as an activity ancillary to their main business should be performed at a group level. In line with Article 2(11) of Directive 2013/34/EU of the European Parliament and of the Council[2], a group is considered to comprise the parent undertaking and all its subsidiary undertakings and includes entities domiciled in the Union and in third countries regardless of whether the group is headquartered inside or outside the Union.

(2) The assessment should be performed in the form of two tests, which are both based on the trading activity of the persons within the group and should be calculated on a per-asset-class basis. The first test should determine whether the persons within the group are large participants relative to the size of the financial market in that asset class and as a consequence should be required to obtain authorisation as an investment firm. The second test should determine whether the persons within the group trade on own account or provide investment services in commodity derivatives, emission allowances or derivatives thereof to such a large extent relative to the main business of the group that those activities cannot be considered to be ancillary at group level and that therefore the persons should be required to obtain authorisation as an investment firm.

(3) The first test compares the size of a person's trading activity against the overall trading activity in the Union on an asset class basis to determine that person's market share. The size of the trading activity should be determined by deducting the sum of the volume of the transactions for the purposes of intra-group liquidity or risk management purposes, objectively measurable reduction of risks directly relating to commercial or treasury financing activity or fulfilling obligations to provide liquidity

[1] OJ L 173, 12.06.2014, p. 349.

[2] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC (OJ L 182, 29.6.2013, p. 19).

on a trading venue ('privileged transactions') from the volume of the overall trading activity undertaken by the person.

(4) The volume of the trading activity should be determined by the gross notional value of contracts in commodity derivatives, emission allowances and derivatives thereof on the basis of a rolling average of the preceding three annual periods. The overall market size should be determined on the basis of trading activity undertaken in the Union in relation to each asset class for which the exemption is sought, including contracts which are traded on and outside trading venues in the Union.

(5) As commodity markets differ significantly in terms of size, number of market participants, level of liquidity and other characteristics, different thresholds shall apply for different asset classes in relation to the test on the size of the trading activity.

(6) The second test provides two methods for determining the size of the trading activity in order to compare it to the size of the main activity undertaken by the group. That test takes two forms in order to better reflect the underlying activities of the persons intending to use the exemption whilst minimising the regulatory burden and complexity of implementing the test. The capital test is provided as an alternative to the trading test in order to take into account of the economic reality of the very heterogeneous groups that need to undertake the assessment whether their trading is ancillary to their main business activities, including groups that undertake significant capital investments, relative to their size, in the creation of infrastructure transportation and production facilities, as well as investments which cannot be easily hedged in financial markets. As both forms of the second test cater for the different underlying economic realities of various groups both tests constitute equally suitable methods to determine whether the trading activity is ancillary to the main business of a particular group.

(7) The size of the trading activity as used under the first method of the second test is taken as a proxy for the commercial activity that the person or group engages in as its main business. This proxy should be easy and cost efficient for persons to apply as it builds on data already required to be collected for the first test while at the same time establishing a meaningful test.

(8) This proxy is appropriate because a rational risk-averse entity, such as a producer, processor or consumer of commodities or emission allowances, is deemed to hedge the volume of the commercial activity of its main business with an equivalent volume of commodity derivatives, emission allowances or derivatives thereof. Therefore the volume of all its trading activity in commodity derivatives, emission allowances or derivatives thereof measured in the gross notional value of the underlying is an appropriate proxy for the size of the main business of the group. As groups whose main business activities are not related to commodities or emission allowances would not use commodity or emission allowances derivatives as a risk-reducing tool, their trading in commodity derivatives, emission allowances or derivatives thereof would not qualify as hedging.

(9) The use of commodity derivatives as a risk-reducing tool however cannot be considered a perfect proxy for all the commercial activity that the person or group conducts as its main business since it may not take into account other investments in fixed assets unrelated to derivative markets. In order to correct the potential mismatch between a group's trading in commodity derivatives and the actual size of its main business with regard, in particular, to small groups the first method of the second test should contain a backstop which recognises that the trading activity undertaken by the

persons within the group should also not exceed a certain percentage of any of the thresholds set under the first test for each relevant asset class to be deemed ancillary. The higher the percentage of speculative activity within all trading activity of a group, the lower the threshold set under the first test.

(10) The backstop based on a group not exceeding a certain percentage of any of the thresholds set under the first test for each relevant asset class is particularly relevant for very small groups with negligible overall footprint in the relevant commodity derivative trading. On the one hand, those groups may be required to undertake a costly analysis of their trading activities to determine whether that trading reduces risk or not without the result being conclusive on the ancillary nature of the trading activity. On the other hand, those groups are usually not equipped to engage in the capital test as an alternative to the test based on trading. In order to avoid disproportionate burdens on those groups, it is appropriate that groups whose trading activity for each relevant asset class accounts for less than one-fifth of the threshold set under the first test be considered as carrying out that trading as an ancillary activity to their main business. The first method under the second test, however, may not adequately measure the main activity of persons who have significant capital investments, relative to their size, in the creation of infrastructure, transportation and production facilities. Neither does it recognise investments which cannot be hedged in financial markets. Therefore it is necessary for the second test to contain a second method that uses a capital based metric to measure that that trading activity is ancillary to the main business of the group.

(11) The second method under the second test uses the estimated capital that a non-financial group would be required to hold against the market risk inherent in its positions arising from trading in commodity derivatives, emission allowances and derivatives thereof, other than those from privileged transactions, as a proxy for the amount of ancillary activities undertaken by the persons in a group. The framework developed under the auspices of the Basel Committee and implemented in the Union through the Capital Requirements Directive is used to apply a proportionate notional capital weighting to positions. Within this framework, the net position in a commodity derivative, emission allowance or derivative thereof shall be determined by netting long and short positions in a particular type of commodity derivative contract, emission allowance or derivative contract thereof, such as a future, option, forward or warrants. In determining the net position, netting should take place irrespective of where the contract is traded, the contract's counterparty or its maturity. The gross position in a relevant commodity derivative, emission allowance contract or a derivative contract thereof should, on the other hand, be calculated by adding the net positions of types of contracts that relate to a particular commodity or, emission allowance or derivative thereof. In this context, net positons in a particular type of commodity derivative contract, emission allowance contract or derivative contract thereof should not be netted against each other.

(12) Under the second method of the second test, the amount of the estimated capital of a group is then compared to the actual amount of capital employed of that group that should reflect the size of its main activity. The capital employed is calculated on the basis of the total assets of the group minus its current debt. Current debt should comprise debt that is due to be settled within twelve months.

(13) The rationale of the ancillary activity tests is to check whether persons within a group that are not authorised in accordance with Directive 2014/65/EU should apply for an authorisation due to the relative or absolute size of their activity in commodity

derivatives, emission allowances and derivatives thereof. The ancillary activity tests thus determine the size of activities in commodity derivatives, emission allowances and derivatives thereof which persons within a group may carry out without authorisation under Directive 2014/65/EU due to those activities being ancillary to the group's main business. It is therefore appropriate to calculate the size of the ancillary activity of the group by using criteria which exclude the activity carried out by group members which are authorised in accordance with that Directive in order to assess the size of genuine ancillary activity carried out by unauthorised group members.

(14) In order to allow for market participants to plan and operate their business in a reasonable way and to take into account seasonal patterns of activity, the calculation of the tests determining when an activity is considered to be ancillary to the main business should be based on a period of three years. Therefore, entities should perform the assessment whether they breach one of the two thresholds on an annual basis by calculating a simple average of three years on a rolling basis in order to be able to submit their annual notification to the competent authority. This obligation should be without prejudice to the right of the competent authority to request at any time a report from a person about the basis on which that person considers its activity under points (i) and (ii) of Article 2(1) (j) of Directive 2014/65/EU to be ancillary to its main business.

(15) Transactions objectively measurable as reducing risks directly relating to commercial activity or treasury financing activity and intra-group transactions should be considered in a way consistent with Regulation (EU) No. 648/2012 of the European Parliament and of the Council[3]. However, in relation to transactions in derivatives which are objectively measurable as reducing risks directly relating to the commercial activity or treasury financing activity Commission Delegated Regulation (EU) No 149/2013[4] only refers to derivatives not traded on regulated markets while Article 2(4) of Directive 2014/65/EU covers derivatives traded on trading venues. Therefore, this Regulation should also take into account derivatives traded on regulated markets in relation to transactions that are deemed to be objectively measurable as reducing risks directly related to commercial or treasury financing activity.

(16) In some circumstances, it may not be possible to hedge a commercial risk by using a directly related commodity derivative contract: a contract with exactly the same underlying and settlement date as the risk being covered. In such case, the person may use proxy hedging through a closely correlated instrument to cover its exposure such as an instrument with a different but very close underlying in terms of economic behaviour. Additionally, macro or portfolio hedging may be used by persons, which enter into commodity derivative contracts to hedge a risk in relation to their overall risks or the overall risks of the group. Those macro, portfolio or proxy hedging commodity derivative contracts may constitute hedging for the purpose of this Regulation.

(17) When a person applying the ancillary activity test uses portfolio or macro hedging, it may not be able to establish a one-to-one link between a specific transaction in a

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[3] Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (OJ L 201, 27.7.2012, p. 1).

[4] Commission Delegated Regulation (EU) No 149/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards on indirect clearing arrangements, the clearing obligation, the public register, access to a trading venue, non-financial counterparties, and risk mitigation techniques for OTC derivatives contracts not cleared by a CCP (OJ L 52, 23.2.2013, p. 11).

commodity derivative and a specific risk directly related to the commercial and treasury financing activities entered into to hedge it. The risks directly related to the commercial and treasury financing activities may be of a complex nature e.g. several geographic markets, several products, time horizons or entities. The portfolio of commodity derivative contracts entered into to mitigate those risks may derive from complex risk management systems. In such cases the risk management systems should prevent non-hedging transactions from being categorised as hedging and provide for a sufficiently disaggregate view of the hedging portfolio so that speculative components are identified and counted towards the thresholds. Positions should not qualify as reducing risks related to commercial activity solely on the grounds that they form part of a risk-reducing portfolio on an overall basis.

(18) A risk may evolve over time and, in order to adapt to the evolution of the risk, commodity or emission allowance derivatives initially executed for reducing risk related to commercial activity, may have to be offset through the use of additional commodity or emission allowance derivative contracts. As a result, hedging of a risk may be achieved by a combination of commodity or emission allowance derivative contracts including offsetting commodity derivative contracts that close out those commodity derivative contracts that have become unrelated to the commercial risk. Additionally the evolution of a risk that has been addressed by the entering into of a position in a commodity or emission allowance derivative for the purpose of reducing that risk should not subsequently give rise to the re-evaluation of that position as being not a privileged transaction ab initio.

(19) This Regulation is based on the draft regulatory technical standards submitted by the European Securities and Markets Authority (ESMA) to the Commission.

(20) ESMA has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Securities and Markets Stakeholder Group established by Article 37 of Regulation (EU) No 1095/2010 of the European Parliament and of the Council[5].

(21) For reasons of consistency and in order to ensure the smooth functioning of the financial markets, it is necessary that the provisions laid down in this Regulation and the related national provisions transposing Directive 2014/65/EU apply from the same date.

HAS ADOPTED THIS REGULATION:

Article 1

Application of thresholds

The activities of persons referred to in points (i) and (ii) of Article 2(1) (j) of Directive 2014/65/EU shall be considered to be ancillary to the main business of the group if those activities meet the conditions set out in Article 2 and constitute a minority of activities at group level in accordance with Article 3.

[5] Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15.12.2010, p. 84).

Article 2

Overall market threshold

1. The size of the activities referred to in Article 1 calculated in accordance with paragraph 2 divided by the overall market trading activity calculated in accordance with paragraph 3 shall, in each of the following asset classes, account for less than the following values:

   (a) 4 % in relation to derivatives on metals;

   (b) 3 % in relation to derivatives on oil and oil products;

   (c) 10 % in relation to derivatives on coal;

   (d) 3 % in relation to derivatives on gas;

   (e) 6 % in relation to derivatives on power;

   (f) 4 % in relation to derivatives on agricultural products;

   (g) 15 % in relation to derivatives on other commodities, including freight and commodities referred to in Section C 10 of Annex I to Directive 2014/65/EU;

   (h) 20 % in relation to emission allowances or derivatives thereof.

2. The size of the activities referred to in Article 1 undertaken in the Union by a person within a group in each of the asset classes referred to in paragraph 1 shall be calculated by aggregating the gross notional value of all contracts within the relevant asset class to which that person is a party.

   The aggregation referred to in the first subparagraph shall not include contracts resulting from transactions referred to in points (a), (b) and (c) of the fifth subparagraph of Article 2(4) of Directive 2014/65/EU or contracts where the person within the group that is a party to any of them is authorised in accordance with Directive 2014/65/EU or Directive 2013/36/EU.

3. The overall market trading activity in each of the asset classes referred to in paragraph 1 shall be calculated by aggregating the gross notional value of all contracts that are not traded on a trading venue within the relevant asset class to which any person located in the Union is a party and of any other contract within that asset class that is traded on a trading venue located in the Union during the relevant annual accounting period referred to in Article 4(2).

4. The aggregate values referred to in paragraphs 2 and 3 shall be denominated in EUR.

Article 3

Main business threshold

1. The activities referred to in Article 1 shall be considered to constitute a minority of activities at group level where they comply with any of the following conditions:

   (a) the size of those activities calculated in accordance with the first subparagraph of paragraph 3 does not account for more than 10% of the total size of the trading activity of the group calculated in accordance with the second subparagraph of paragraph 3;

(b) the estimated capital employed for carrying out those activities calculated in accordance with paragraphs 5 to 7 does not account for more than 10% of the capital employed at group level for carrying out the main business calculated in accordance with paragraph 9.

2. The following derogations from paragraph 1(a) shall apply:

(a) where the size of the activities referred to in Article 1 calculated in accordance with the first subparagraph of paragraph 3 accounts for more than 10% but less than 50% of the total size of the trading activity of the group calculated in accordance with the second subparagraph of paragraph 3, ancillary activities shall be considered to constitute a minority of activities at group level only where the size of the trading activity for each of the asset classes referred to in Article 2(1) accounts for less than 50% of the threshold established by Article 2(1) for each relevant asset class;

(b) where the size of the trading activities calculated in accordance with the first subparagraph of paragraph 3 accounts for equal to or more than 50% of the total size of the trading activity of the group calculated in accordance with the second subparagraph of paragraph 3, ancillary activities shall be considered to constitute a minority of activities at group level only where the size of the trading activity for each of the asset classes referred to in Article 2(1) accounts for less than 20% of the threshold established by Article 2(1) for each relevant asset class.

3. The size of the activities referred to in Article 1 undertaken by a person within a group shall be calculated by aggregating the size of the activities undertaken by that person with respect to all of the asset classes referred to in Article 2(1) in accordance with the same calculation criteria as that referred to in Article 2(2).

The total size of the trading activity of the group shall be calculated by aggregating the gross notional value of all contracts in commodity derivatives, emission allowances and derivatives thereof to which persons within that group are a party to.

4. The aggregation referred to in the first subparagraph of paragraph 3 shall not include contracts where the person within the group that is a party to any of those contracts is authorised in accordance with Directive 2014/65/EU or Directive 2013/36/EU.

5. The estimated capital employed for carrying out the activities referred to in Article 1 shall be the sum of the following:

(a) 15 % of each net position, long or short, multiplied by the price for the commodity derivative, emission allowance or derivatives thereof;

(b) 3 % of the gross position, long plus short, multiplied by the price for the commodity derivative, emission allowance or derivatives thereof.

6. For the purposes of paragraph 5, point (a), the net position in a commodity derivative, an emission allowance or derivative thereof shall be determined by netting long and short positions:

(a) in each type of commodity derivative contract with a particular commodity as underlying in order to calculate the net position per type of contract with that commodity as underlying;

(b) in an emission allowance contract in order to calculate the net position in that emission allowances contract; or

(c) in each type of emission allowance derivative contract in order to calculate the net position per type of emission allowance derivative contract.

For the purposes of paragraph 5, point (a), net positions in different types of contracts with the same commodity as underlying or different types of derivative contracts with the same emission allowance as underlying can be netted against each other.

7. For the purposes of paragraph 5, point (b), the gross position in a commodity derivative, an emission allowance or a derivative contract thereof, shall be determined by computing the sum of the absolute values of the net positions per type of contract with a particular commodity as the underlying, per emission allowance contract or per type of contract with a particular emission allowance as the underlying.

For the purposes of paragraph 5, point (b), net positions in different types of derivative contracts with the same commodity as underlying or different types of derivative contracts with the same emission allowance as underlying cannot be netted against each other.

8. The calculation of the estimated capital shall not include positions resulting from transactions referred to in points (a), (b) and (c) of subparagraph 5 of Article 2(4) of Directive 2014/65/EU.

9. The capital employed for carrying out the main business of a group shall be the sum of the total assets of the group minus its short-term debt as recorded in its consolidated financial statements of the group at the end of the relevant annual calculation period. For the purposes of the first sentence, short-term debt means debt with a maturity of less than 12 months.

10. The values resulting from the calculations referred to in this Article shall be denominated in EUR.

Article 4

Procedure for calculation

1. The calculation of the size of the trading activities and capital referred to in Articles 2 and 3 shall be based on a simple average of the daily trading activities or estimated capital allocated to such trading activities, during three annual calculation periods that precede the date of calculation. The calculations shall be carried out annually in the first quarter of the calendar year that follows an annual calculation period.

2. For the purpose of paragraph 1, an annual calculation period means a period which starts on 1 January of a given year and ends on 31 December of that year.

3. For the purpose of paragraph 1, the calculation of the size of trading activities or estimated capital allocated to trading activities taking place in 2018 shall take into account the three preceding annual calculation periods, starting on 1 January 2015, 1 January 2016 and 1 January 2017, and the calculation taking place in 2019 shall take into account the three preceding annual calculation periods, starting on 1 January 2016, 1 January 2017 and 1 January 2018.

4. By derogation to paragraph 3, the reference period for the calculation of daily trading activities or estimated capital allocated to such trading activities shall comprise only the most recent annual calculation period when the following conditions are met:

(a) daily trading activities or estimated capital allocated to such trading activities declines by more than 10%, when comparing the earliest of the three preceding annual calculation periods with the most recent annual calculation period; and

(b) daily trading activities or estimated capital allocated to such trading activities in the most recent of the three annual calculation periods is lower than in the two preceding calculation periods.

Article 5

Transactions qualifying as reducing risks

1. For the purposes of point (b) of the fifth subparagraph of Article 2(4) of Directive 2014/65/EU, a transaction in derivatives shall be considered objectively measurable as reducing risks directly relating to the commercial activity or treasury financing activity when one or more of the following criteria is met:

(a) the transaction reduces the risks arising from the potential change in the value of assets, services, inputs, products, commodities or liabilities that the person or its group owns, produces, manufactures, processes, provides, purchases, merchandises, leases, sells, or incurs or reasonably anticipates owning, producing, manufacturing, processing, providing, purchasing, merchandising, leasing, selling or incurring in the normal course of its business;

(b) the transaction covers the risks arising from the potential indirect impact on the value of assets, services, inputs, products, commodities or liabilities referred to in point (a), resulting from fluctuation of interest rates, inflation rates, foreign exchange rates or credit risk;

(c) the transaction qualifies as a hedging contract pursuant to International Financial Reporting Standards adopted in accordance with Article 3 of Regulation (EC) No 1606/2002 of the European Parliament and Council.

2. For the purposes of paragraph 1, a qualifying risk-reducing transaction taken on its own or in combination with other derivatives is one for which a non-financial entity:

(a) describes the following in its internal policies:

(i) the types of commodity derivative , emission allowance or derivative thereof contracts included in the portfolios used to reduce risks directly relating to commercial activity or treasury financing activity and their eligibility criteria;

(ii) the link between the portfolio and the risks that the portfolio is mitigating;

(iii) the measures adopted to ensure that the transactions concerning those contracts serve no other purpose than covering risks directly related to the commercial activity or the treasury financing activity of the non-financial entity, and that any transaction serving a different purpose can be clearly identified;

(b) is able to provide a sufficiently disaggregate view of the portfolios in terms of class of commodity derivative, emission allowance or derivative thereof, underlying commodity, time horizon and any other relevant factors.

Article 6

Entry into force and application

1. This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

2. This regulation shall apply from 3 January 2018.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 1.12.2016

For the Commission
The President
Jean-Claude JUNCKER