Review of the Markets in Financial Instruments Directive Questionnaire on MiFID/MiFIR 2 by Markus Ferber MEP

The questionnaire takes as its starting point the Commission's proposals for MiFID/MiFIR 2 of 20 October 2011 (COM(2011)0652 and COM(2011)0656).

All interested stakeholders are invited to complete the questionnaire. You are invited to answer the following questions and to provide any detailed comments on specific Articles in the table below. Responses which are not provided in this format may not be reviewed. Respondents to this questionnaire should be aware that responses may be published. Please send your answers to econ-secretariat@europarl.europa.eu **by 13 January 2012.**

Name of the person/ organisation responding to the questionnaire	**BDEW** The German Association of Energy and Water Industries (Bundesverband der Energie- und Wasserwirtschaft-BDEW), Berlin, represents the interests of approximately 1,800 companies. The spectrum of its members ranges from local and municipal to regional and interregional companies. They represent about 90 percent of electricity sales, more than 60 percent of local and district heat supply, 90 percent of natural gas sales as well as 80 percent of drinking water abstraction and about one third of wastewater disposal in Germany. **Introductory Remark:** BDEW supports the activities to increase the stability of financial markets and to ensure the confidence in their functioning. We agree with the goals identified in the G20 summit of April 2009. Their correct implementation is important for overall welfare and economic stability. Extending the scope of the MiFID would make the MiFID licence a mandatory requirement for dealing at energy

	wholesale markets. This would significantly impact the successful development of a competitive energy wholesale market. The costs and organisational effects of the licence are likely to push many of our approximately 1,800 member companies out of this market altogether. This includes even larger municipal utilities as well as small and medium-sized energy companies. Furthermore, with an extension of the rules of MiFID, the EMIR and CRD IV application becomes fully mandatory for those energy companies, which will continue to be active at wholesale markets. The proposed changes endanger competition and liquidity energy wholesale markets. With the existing REMIT (Regulation on Wholesale Energy Markets Integrity and Transparency) regime and the forthcoming EMIR obligations for non-financial counterparties, there are effective and efficient oversight regimes, and we therefore propose that companies that fall under REMIT and are below the systemic threshold for non-financials under EMIR, should be exempt from MiFID by definition.

Theme	Question	Answers
Scope	1) Are the exemptions proposed in Directive Articles 2 and 3 appropriate? Are there ways in which more could be done to exempt corporate end users?	**Deletion of exemption for Commodity Dealers (Art. 2.1.k):** BDEW is very concerned about the current approach to expand the scope of MiFID particularly for commodity derivative dealers. With the proposed deletion of the specific exemption, BDEW fears that a significant number of our member companies, including generators, electricity/ gas suppliers would either be forced to acquire a MiFID license or would be forced out of the wholesale trading market – hence lose market shares in the physical market. For our member companies, also trading in forward electricity and/or gas, as well as auctioning forward transport capacity is at the core of the physical process. In addition, energy companies as represented by BDEW are not systemically relevant for financial markets. **Exemption for ancillary activities (Art. 2.1.i):** BDEW appreciates the general notion of Art. 2.1.i, which could provide the basis for an appropriate treatment of energy companies, but urges for further clarification in order to accommodate functioning energy markets. The exemption has to be broadened and clarified as the energy firms should remain fully exempt from MiFID II provided that they trade primarily to manage their and their clients' commercial positions and commodity price risks (e.g. managing the generation portfolio, sales portfolio and residual positions) or, in the case of emissions allowances,

		to meet their compliance requirements and optimise their compliance portfolio on an individual entity or group basis. The proposal indicates that the EU Commission shall adopt delegated acts to specify the conditions that will determine whether the trading activity of a company is ancillary to its main business. This proposal recognises that companies involved in the physical production, supply and consumption of commodities (e.g. power and gas) are active in derivatives trading to manage commercial risks as described above, and that such commercial trades should remain exempt from financial regulation. The same shall apply to services provided to clients of the energy company. However, the presumption should be that energy firms and their energy trading subsidiaries can remain fully exempt from MiFID II provided that they trade primarily to manage the commercial positions and commodity price risks or, in the case of emissions allowances, to meet their compliance requirements and optimise their compliance portfolio on an individual entity or group basis (recital 88). This objective should be translated into clear legal language, for instance clarifying that all trading activities in instruments used for the commercial activities will be possible without being licensed. Besides the above mentioned clarification, the words "excluding persons who deal on own account by executing client orders" have to be deleted, because the wording is unclear and the application could have detrimental effects on the main aims of MiFID, i.e. investor protection. In addition, a certain level of proprietary trading activities should be permissible without being subject to the MiFID II licensing requirements

		provided it does not create any systemic risk. This ensures that non-financial firms are treated in the same manner under MiFID II and EMIR and do not become classified as financial institutions. This is important in particular for middle-sized as well as small-sized energy trading companies that are created to support risk management on behalf of the owners, as this activity is ancillary to the owners' main business supply of energy. **BDEW Proposals:** "ancillary services" should be defined as (a) dealing on one's own account with transactions in financial instruments which are entered into by a non-financial counterparty that are objectively measurable as directly related to the commercial or treasury financing activities of that counterparty or the commercial or treasury financing activities of other non-financial entities within the group to which the non financial counterparty belongs, or (b) dealing on one's own account in financial instruments of such non financial counterparties as referred to in article 2 (7) of Regulation ---/--- [EMIR], that are not exceeding the clearing threshold as defined in article 7 (3) of Regulation ---/--- [EMIR] Additionally, BDEW believes that the notion "client" should be made clearer and proposes that (a) a client is to be considered on a group basis, (b) a client can be a counterparty concluding a physical contract (thereby becoming a client) and receiving financial services at the same time; thus the client relationship does not necessarily have to exist prior to receiving the financial service. (c) For the exemption to apply, there does not have to be a precise

		nexus between a physical contract with the client and a financial service to the client, it suffices to require the financial service to serve the purpose of managing a commercial positions and/ or commodity price risks of the client. The reason being that the management of commercial positions and commodity price risks is not any longer a one-on-one system but of complex nature. The prerequisite of “sachlicher Zusammenhang” (factual coherence) in § 2 VI No. 11.c KWG (German “Kreditwesengesetz”) had gone beyond Mifid I and prevents reasonable handling of the exemption. **Exemption for TSOs (Art. 2.1.n):** BDEW welcomes the exemption for TSOs as adequate. However, the same should apply to distribution system operators and “storage and LNG System Operators” according to Directive 2009/73/EC. The platform for storage capacities (store-x) is currently in progress of extending services and without a clear exemption its further development would be hindered. **Exemption for trading on own account (Art. 2.1.d)** BDEW regards the revised exemption as (with the inclusion of an additional criterion) too narrow for energy firms, i.e. cannot be used at all. Most energy companies are a member of or a participant in a regulated market (e.g. European Energy Exchange) or MTF (Multilateral Trading Platforms). Therefore, the wording of the exemption (2(1)(d) (ii)) needs to be improved in order to better clarify the intention to include in MiFID only high-frequency/algorithmic traders and not all market participants or

		members of regulated markets or MTFs. As a clarification is needed to ensure that the inclusion in any of the exemptions defined is not affected by partial exclusions defined under other exemptions (‘cumulative application’) (this is important to avoid uncertainty, for instance, for firms that can benefit from the ancillary activity exemption but that at the same time are market makers or members or participants of regulated markets or MTFs), we propose the according clarification in the last sentence of Art. 2 (1) (d)). **Exemption for hedging purposes (Art. 2.1.k)** BDEW proposes a further clarification in the new Art 2.1.(k) as follows: firms (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;
	2) Is it appropriate to include emission allowances and structured deposits and have they been included in an appropriate way?	**Emission allowances:** Although EUAs do share some common features with other classes of financial instruments, such as transferable securities (e.g. dematerialised

		bearer bonds held in a clearing system), they are distinguishable from such types of financial instrument for several reasons: they do not confer financial claims against the public issuer of such allowances; and they do not represent titles to capital or title to debentures or constitute forward contracts. Emission allowances are designed to serve climate change objectives and their primary purpose is not to serve as an investment instrument. Hence, BDEW regards it as inappropriate to classify emission allowances as financial instruments. Many BDEW member companies, as compliance buyers, will run the risk that their balances become inadequately volatile, as emission allowances are considered input factors for the energy production and valued on the basis of market mechanisms. Moreover, the liquidity of the EUA-market would be expected to decrease. Trading conditions for independent traders would become more difficult and reduce their activities. Companies concerned would solely focus on compliance activities to ensure they are exempted under Art. 2.1.i. **Alternative approach:** BDEW proposes that emission allowances are not included and that instead specific market integrity measures should be introduced outside of MiFID in order to protect market functioning and investors.
	3) Are any further adjustments needed to reflect the inclusion of custody and safekeeping as a core service?	The deletion of Art. 2.1.k will be highly relevant to energy firms which operate energy trading by unconsolidated subsidiaries:

		As they relied mainly on the exemption of commodity derivatives (Art. 2.1.k), it now becomes crucial which group structure will be eligible for exemptions. The definition of parent undertakings/ subsidiaries (Art. 2.1.b referring to Art. 4.1.b) is deficient as subsidiaries which are owned by several shareholder will not be eligible. BDEW therefore proposes to expand the exemption to jointly managed undertakings as defined in Art. 32 of the Seventh Council Directive 83/349/EEC of 13 June 1983.
	4) Is it appropriate to regulate third country access to EU markets and, if so, what principles should be followed and what precedents should inform the approach and why?	BDEW welcomes the proposal that firms from third countries for which an equivalent decision has been adopted would be able to request to provide services in the EU. However, the assessment of whether the regulatory regime of a third country is equivalent should not be based on strictly identical financial regimes, because no two regulatory regimes are identical in all respects. Therefore, we propose that equivalence should be defined in terms of intent rather than in terms of specific rules, at the same time preventing opportunities for regulatory arbitrage.
Corporate governance	5) What changes, if any, are needed to the new requirements on corporate governance for investment firms and trading venues in Directive Articles 9 and 48 and for data service providers in Directive Article 65 to ensure that they are proportionate and effective, and why?	
Organisation of markets and trading	6) Is the Organised Trading Facility category appropriately defined and differentiated from other trading venues and from systematic internalisers in	The new proposals have rightly recognized that physically settled OTC commodity forward products should not be classified as financial instruments (see Annex 1, C(7)).

	the proposal? If not, what changes are needed and why?	However, they fail to fully clarify the distinction between financial instruments and physical contracts (in Annex 1, C (6)). Indeed financial instruments are subject to MiFID II and associated regulations whilst physical OTC contracts remain exempt from MiFID II, but can be subject to sector-specific regulations, for example REMIT (Regulation on Wholesale Energy Market Integrity and Transparency). BDEW is very concerned, that the amended Annex 1, C (6) classifies a contract that is settled physically and traded on an organized trading facility (OTF) improperly as a financial instrument. Use of physically settled forward products is essential for commercial firms. Their inclusion under MiFID II would effectively extend the scope of MiFID II to purely commercial activities (i.e. gas/power contracts including physical delivery) which do not display the characteristics of traditional derivatives trading. This would reduce substantially the scope of the ancillary activity exemption as this type of trading typically represents the main trading activity of energy firms. As such, it is essential that physically settled contracts remain outside the scope of the directive. In addition this has considerable implications regarding the framework of non financial firms under EMIR and the enforcement of position limits, position reporting and equivalent measures.
	7) How should OTC trading be defined? Will the proposals, including the new OTF category, lead to the channelling of trades which are currently OTC	The proposal fails to fully clarify the distinction between financial instruments and physical contracts under the amended No 6 of Annex 1,

	onto organised venues and, if so, which type of venue?	section C. Accordingly, the amended Annex 1, C (6) would classify a contract that is settled physically and traded on an organised trading facility (OTF) improperly as a financial instrument, which would be inappropriate for the energy wholesale markets. The use of physically settled forward products is essential for commercial firms. Their inclusion under MiFID II would effectively extend the scope of MiFID II to purely commercial activities (i.e. gas/power contracts including physical delivery) which do not display the characteristics of traditional derivatives trading. This would reduce substantially the scope of the ancillary activity exemption as this type of trading typically represents the main trading activity of energy firms. As such, it is essential that physically settled contracts remain outside the scope of the directive. BDEW supports a better specification of the MiFID II perimeter to exclude all products with future delivery that are physically settled from the definition of financial instruments. (This is the approach used in the US under the Dodd-Frank Act, and as such any departure from this approach in the EU would create regulatory inconsistency. We propose that the "commercial purpose test" (of Annex 1, C (7) is also applied to physically settled forwards traded over regulated markets, MTFs and OTFs (into Annex 1, C (7)) to filter out commercial activities from the definition of financial instruments.)
	8) How appropriately do the specific requirements related to algorithmic trading, direct electronic access and co-location in Directive Articles 17, 19, 20 and 51 address the risks involved?	

	9) How appropriately do the requirements on resilience, contingency arrangements and business continuity arrangements in Directive Articles 18, 19, 20 and 51 address the risks involved?	
	10) How appropriate are the requirements for investment firms to keep records of all trades on own account as well as for execution of client orders, and why?	
	11) What is your view of the requirement in Title V of the Regulation for specified derivatives to be traded on organised venues and are there any adjustments needed to make the requirement practical to apply?	
	12) Will SME gain a better access to capital market through the introduction of an MTF SME growth market as foreseen in Article 35 of the Directive?	
	13) Are the provisions on non-discriminatory access to market infrastructure and to benchmarks in Title VI sufficient to provide for effective competition between providers? If not, what else is needed and why? Do the proposals fit appropriately with EMIR?	
	14) What is your view of the powers to impose position limits, alternative arrangements with equivalent effect or manage positions in relation to commodity	BDEW clearly opposes the introduction of position limits for energy markets. Such limits cannot be executed in the optimisation of natural positions,

	derivatives or the underlying commodity? Are there any changes which could make the requirements easier to apply or less onerous in practice? Are there alternative approaches to protecting producers and consumers which could be considered as well or instead?	such as a long position of a power plant. Physical optimisation which secures the real economy cannot be covered by position limits. Position limits might only be adequate for the financial economy. They can affect market liquidity and thus increase price volatility. **BDEW Proposal:** At least clear provisions to exempt risk management activities are needed. This can be done by defining that commercial firms shall not be subject to position limits for those products that are used for risk management activities. Position limits should remain a tool of last resort where there is strong evidence of market failure.
Investor protection	15) Are the new requirements in Directive Article 24 on independent advice and on portfolio management sufficient to protect investors from conflicts of interest in the provision of such services?	
	16) How appropriate is the proposal in Directive Article 25 on which products are complex and which are non-complex products, and why?	
	17) What if any changes are needed to the scope of the best execution requirements in Directive Article 27 or to the supporting requirements on execution quality to ensure that best execution is achieved for clients without undue cost?	
	18) Are the protections available to eligible counterparties, professional clients and retail clients	

	appropriately differentiated?	
	19) Are any adjustments needed to the powers in the Regulation on product intervention to ensure appropriate protection of investors and market integrity without unduly damaging financial markets?	
Transparency	20) Are any adjustments needed to the pre-trade transparency requirements for shares, depositary receipts, ETFs, certificates and similar in Regulation Articles 3, 4 and 13 to make them workable in practice? If so what changes are needed and why?	
	21) Are any changes needed to the pre-trade transparency requirements in Regulation Articles 7, 8, 17 for all organised trading venues for bonds, structured products, emission allowances and derivatives to ensure they are appropriate to the different instruments? Which instruments are the highest priority for the introduction of pre-trade transparency requirements and why?	
	22) Are the pre-trade transparency requirements in Regulation Articles 7, 8 and 17 for trading venues for bonds, structured products, emission allowances and derivatives appropriate? How can there be appropriate calibration for each instrument? Will these proposals ensure the correct level of	

	transparency?	
	23) Are the envisaged waivers from pre-trade transparency requirements for trading venues appropriate and why?	
	24) What is your view on the data service provider provisions (Articles 61 - 68 in MiFID), Consolidated Tape Provider (CTPs), Approved Reporting Mechanism (ARMs), Authorised Publication Authorities (APAs)?	
	25) What changes if any are needed to the post-trade transparency requirements by trading venues and investment firms to ensure that market participants can access timely, reliable information at reasonable cost, and that competent authorities receive the right data?	
Horizontal issues	26) How could better use be made of the European Supervisory Authorities, including the Joint Committee, in developing and implementing MiFID/MiFIR 2?	
	27) Are any changes needed to the proposal to ensure that competent authorities can supervise the requirements effectively, efficiently and proportionately?	

	28) What are the key interactions with other EU financial services legislation that need to be considered in developing MiFID/MiFIR 2?	› CRD (Capital Requirements Directive) -> this is the major burden for energy companies covered by MiFID! Thus we strongly ask for a joint approach (and not an independent revision of the two major directives) › EMIR (OTC Derivatives Regulation) › MAD (as the scope of REMIT also depends on the definition of financial instruments)
	29) Which, if any, interactions with similar requirements in major jurisdictions outside the EU need to be borne in mind and why?	Financial Market Regulation in the USA
	30) Is the sanctions regime foreseen in Articles 73-78 of the Directive effective, proportionate and dissuasive?	
	31) Is there an appropriate balance between Level 1 and Level 2 measures within MIFID/MIFIR 2?	

Detailed comments on specific articles of the draft Directive

Article number	**Comments**
Article 2.1 :	The reasoning for BDEW's plea to further develop and improve the exemption in Art. 2.1.i as mentioned above is • the need for greater clarity and certainty for market participants and • of consistency of application across Member States and

	• the following chain of reasoning: ➢ If an energy company will not be able to use the exemptions under MiFID II, it becomes subject to (a) a MiFID II licensing regime by becoming an investment firm and, (b) therefore, to (i) a multitude or organizational requirements under MiFID, (ii) central clearing requirements under EMIR (OTC Derivatives Regulation) and (iii) capital adequacy requirements under CRD (if the current CRD exemptions are not adequately prolonged before the . expiring date end of 2014). All these sets of rules increase costs in administration and by requiring companies to have larger amount of capital and collateral available to support their trading activities; In addition, the mandatory CCP clearing triggers substantial liquidity risks for energy firms. An increase in costs and liquidity risks would, in turn, discourage hedging, reduce liquidity and divert capital away from physical investments as well as increase energy prices substantially. Furthermore, as an investment firm it will become subject to mandatory platform trading. ➢ The combination of these effects would ultimately slow down /endanger the development of the internal energy market and the achievement of EU decarbonisation policies.
Article ... :	