Review of the Markets in Financial Instruments Directive

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).

Questionnaire on MiFID/MiFIR 2 by Markus Ferber MEP

E.ON AG response

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?	• E.ON welcomes the EU Commission purpose expressed in the recitals (88) 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*" from MiFID. • The presumption should be that energy firms can remain fully exempt from MiFID II provided that trading is conducted primarily to manage commercial positions and price commodity risks or, in the case of emissions allowances, to service compliance requirements and optimise compliance portfolio on an individual entity or group basis. This objective should be translated into clear legal language within the Directive. • The amendments to the ancillary activity exemption clause (art. 2(1)(i)) proposed in MiFID II are positive, but we are concerned that they might still lend to restrictive or inconsistent interpretations. This can be clarified by stating that all trading activities in instruments used for the commercial activities will be possible to conduct without being licensed under MiFID.

		• Additionally the wording of the exemption 2(1)(d) which excludes persons "that are a member of, or a participant, in a regulated market or MTF" makes the exemption very narrow. In general, almost all market participants are participants of regulated markets or MTF. If the purpose is to make sure that this exemption does not benefit computer/algorithmic traders then this should be clearly stated (see section on specific comments). • Finally a clarification is needed, possibly in the recitals, 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 undue uncertainty.
	2) Is it appropriate to include emission allowances and structured deposits and have they been included in an appropriate way?	• E.ON believes that the proposal to define Emission Allowances (EU Allowances - EUAs, Certified Emission Reductions – CERs - and Emission Reduction Units - ERUs) as a separate class of financial instruments in MiFID II is not appropriate. Although Emission Allowances 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; 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 product.
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 proposal? If not, what changes are needed and why?	• The distinction between OTFs and other types of trading venues is motivated by the Commission with discretionary powers in trade execution for OTFs, not allowed to MTFs. However it is unclear what implication might have the introduction of this new type of platforms, in particular with regard to the energy business. • The foreseeable consequences can be very relevant, however the impact assessment provided by the EU Commission fails to provide sensible details and we believe

		that the potential impacts can be widely underestimated.

	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 onto organised venues and, if so, which type of venue?	• OTC trading should continue to be defined as trading outside regulated markets, as currently defined in MiFID. Therefore off-exchange trading should still be considered OTC. • We notice that the introduction of OTFs may reduce the scope for bespoke contracts. • We are concerned that the amendments to Annex 1, C (6) may improperly lead to a classification of a contract that is settled physically and traded on an organised trading facility (OTF) as a financial instrument. We believe that it shall be possible to trade physical energy contracts in an efficient way without having them defined as financial instruments. If this change is not done in Annex 1, C we see the risk that physical trading is moved from today's' efficient broker platforms to bilateral trading. We believe that this development is more likely than channelling of trades which are currently OTC onto organised venues and lead to inefficient trading as the benefits of broker trading platforms might be strongly weakened. • More importantly the Commission proposals fail to clarify the distinction between financial instruments and physical contracts. Indeed financial instruments are subject to MiFID II and associated regulations whilst physical OTC contracts should remain exempt from MiFID II, but can be subject to sector-specific regulations as Regulation 2011/1227/EC for power and gas. . • Physically settled forward products in particular are of primary use for commercial firms. Any enlargement of the definition of financial instrument would considerably increase the scope of MiFID II to pure commercial activities (i.e. gas/power contracts which aim at the physical delivery) which do not display the characteristics of traditional derivatives. • This may also reduce substantially the scope of the ancillary activity exemption as

		this commercial activity is normally the main non-financial activity of energy firms, but would be regarded wrongly as its main financial trading business (i.e. trading with financial instruments). • In addition this has considerable implications regarding the framework of non financial firms under EMIR and the enforcement of position limits and position reporting. • E.ON strongly supports a better specification of the MiFID II perimeter to exclude from the definition of financial instruments all products with delivery in the future that are physically settled (see section on detailed comments). With this in mind we recall also article 38 of MiFID implementing Regulation 1287/2006/EC (*Characteristics of other derivative financial instruments*), where it is given a clear definition of specific and cumulative conditions that must be met by instruments included in Annex C(7) and C(10) to be defined as derivative financial instruments. • A similar approach has been used in the US under the Dodd-Frank Act, and as such any departure from this approach in the EU would create regulatory inconsistency.
	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?	• The "trading obligation procedure" defined in MiFIR (art 26) provides that the class of derivatives (or a relevant subset thereof) considered sufficiently liquid should be traded only on organised venues i.e. regulated markets, MTFs or OTFs. This procedure may reduce considerably the flexibility available for non financial counterparties below the so called "clearing threshold" defined in EMIR which should remain exempt from mandatory platform trading and mandatory clearing. • E.ON believes that there shall be no mandatory platform trading obligation for wholesale energy products since appropriate supervision and oversight has been introduced with Regulation No. 2011/1227/EC (see section on detailed comments).

		• Besides this obligation may have an indirect impact on all counterparties increasing trading costs.
	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?	• We welcome rules to ensure non-discriminatory access to market infrastructures. We believe that rules on conditions to access central counterparties and trading venues should be very clear and should not remain exclusively theoretical. In particular any refuse to provide access should be duly motivated.
	14) What is your view of the powers to impose position limits, alternative arrangements with equivalent effect or manage positions in relation to commodity 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?	• E.ON does not support the empowerment of regulated platforms (e.g. exchanges) and regulators to establish ex-ante position limits in respect of commodity derivatives. • Position limits hinder effective risk management as companies would be allowed to manage their commodity price risks only up to a certain level. These limits hamper energy suppliers, for example, in forward selling their electricity production to a sufficient extent (via exchanges), or being able to buy in the emissions certificates required to produce electricity • E.ON is in favour of position management supported by appropriate position reporting rather than position limits: we believe that regulatory supervision of positions is a sufficient measure to ensure the proper functioning of markets. Position limits should be a tool of last resort where there is strong evidence of market failure. • At the very 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. This would as well avoid the significant administrative burden for commercial undertakings that have to justify the positions needed for risk management purposes. • Also, the imposition of position reporting in real time on commercial firms active as participants or members on regulated trading platforms is too ambitious and alternative, proportionate arrangements have to be introduced, i.e. that the operators of these platforms will report on behalf of these firms and that market participants would be required to report on a weekly basis only positions in contracts not concluded through platforms as the information should be the basis for the weekly reports done by platforms.
Horizontal issues	28) What are the key interactions with other EU financial services legislation that need to be considered in developing MiFID/MiFIR 2?	• The main financial services legislations that have interactions with MiFID/MiFIR 2 are the European Market Infrastructure Regulation (EMIR), the Capital Requirements Directive (CRD) and the Market Abuse Regulation (MAR). All these are currently under discussion in the legislative process. • In particular we believe that MiFID should be based on provisions agreed in EMIR, when defining rules for non financial counterparties, otherwise the approach of the clearing threshold agreed in EMIR would be overtaken. • Beyond the financial services legislation interactions are foreseen with sector specific legislation in the energy market. In particular the Regulation 2011/1227/EC recently entered into force introduced a single oversight regime for gas and electricity markets and market participants across the entire EU. Regulation no. 1227 includes rules on registration of market participants, prohibition of insider dealing and market manipulation, transaction reporting, monitoring and enforcement powers for National Regulatory Agencies supported by the Agency for Cooperation of Energy Regulators (ACER).

	29) Which, if any, interactions with similar requirements in major jurisdictions outside the EU need to be borne in mind and why?	• We highlight in particular rules concerning the energy sector included in the Dodd-Frank Act approved in the US. E.ON strongly supports a better specification of the MiFID II perimeter to exclude from the definition of financial instruments all products with delivery in the future that are physically settled. 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 (see also answer to 7)

Detailed comments on specific articles of the draft Directive	
Article number	**Comments**
Article2.1 d)	MiFID should enable firms which are not market makers and are not executing orders and are not algorithmic or high-frequency traders, to trade on own account on Regulated Markets or MTFs without becoming subject to MiFID. This proprietary activity is not an investment service for third parties, does not involve executing client orders (i.e. not a systemic internaliser), it is not causing investor protection concerns and it is not of systemic relevance. This kind of activity does not cause the potential risks of algorithmic or high-frequency trading and, hence, need not to be addressed by specific risk controls. In addition the wording of the clarification included in the last paragraph should be better calibrated to avoid misunderstandings *Text proposed by the Commission* / *Amendment* (d) persons who do not provide any investment services or activities other than dealing on own account unless they / (d) persons who do not provide any investment services or activities other than dealing on own account unless they (a) are market makers; / (a) are market makers; (b) ð are a member of or a participant in a regulated market or MTF or / (b) ð are a member of or a participant in a regulated market or MTF or (c) deal on own account by executing client orders ~~outside a regulated market or an MTF on an organised, frequent and systematic basis by providing a system accessible to third parties in order~~ / (c) deal on own account by executing client orders ~~outside a regulated market or an MTF on an organised, frequent and systematic basis by providing a system accessible to third parties in order~~

	~~to engage in dealings with them~~;	~~to engage in dealings with them~~;
	ð 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; □	ð 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 any other applicable exemption as long as the activity does not constitute algorithmic or high-frequency trading***; □
Article 2.3	The elements to be considered in order to define an activity as ancillary to the main business should be clarified, in particular given the fact that the 'ancillary test' should apply (see amendment #2) only to the provision of investment services to the clients of the main business and this activity should be subject to oversight to ensure investor protection.	
	Text proposed by the Commission	*Amendment*
	3. ð The Commission shall adopt delegated acts in accordance with Article 94 concerning measures □ ~~In order to take account of developments on financial markets, and to ensure the uniform application of this Directive, the Commission may ,~~ in respect of exemptions (c) and (i), to ~~and (k) define the criteria for determining~~ clarifying when an	3. ð The Commission shall adopt delegated acts in accordance with Article 94 concerning measures □ ~~In order to take account of developments on financial markets, and to ensure the uniform application of this Directive, the Commission may ,~~ in respect of exemptions (c) and (i), to ~~and (k) define the criteria for determining~~ clarifying when an

		activity is to be considered as ancillary to the main business on a group level as well as for determining when an activity is provided in an incidental manner. ò new 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,*** - the capital employed for carrying out the activity.	activity is to be considered as ancillary to the main business on a group level as well as for determining when an activity is provided in an incidental manner. ò new The criteria for determining whether an activity is ancillary to the main business shall take into account at least the following elements: ***- trading in all financial instruments that are related to risk management of the main business, when considered on a group basis or for the owners in case of joint trading entities, shall be considered as ancillary activity;*** - the capital employed for carrying out the activity ***compared with the capital employed for the main business*** .
Article 2	It should be made clear that the exemptions are cumulative. For example, a treasury company within a group may provide investment services to other group companies covered by article 2(1)(b) but also deal on own account to hedge the group's business risks in ways that would otherwise be covered by article 2(1)(i), therefore any limitation included in one exemption should not interfere with the applicability of any other exemption		
		Text proposed by the Commission	*Amendment*
			1a. An exemption in paragraph 1 that is limited to persons providing particular investment services or performing particular investment activities shall apply to a person even if that person provides

		investment services or performs investment activities covered by another exemption.
Article 59	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. This would as well avoid the significant administrative burden for commercial undertakings that have to justify the positions needed for risk management purposes: *Text proposed by the Commission* 1. Member States shall ensure that regulated markets, operators of MTFs and OTFs which admit to trading or trade commodity derivatives apply limits on the number of contracts which any given market members or participants can enter into over a specified period of time, or alternative arrangements with equivalent effect such as position management with automatic review thresholds , to be imposed in order to: (a) support liquidity; (b) prevent market abuse; (c) support orderly pricing and settlement conditions. The limits or arrangements shall be	*Amendment* 1. Member States shall ensure that regulated markets, operators of MTFs and OTFs which admit to trading or trade commodity derivatives apply limits on the number of contracts which any given market members or participants can enter into over a specified period of time, or alternative arrangements with equivalent effect such as position management with automatic review thresholds , to be imposed in order to: (a) support liquidity; (b) prevent market abuse; (c) support orderly pricing and settlement conditions. The limits or arrangements shall be

		transparent and non-discriminatory, specifying the persons to whom they apply and any exemptions, and taking account of the nature and composition of market participants and of the use they make of the contracts admitted to trading. They shall specify clear quantitative thresholds such as the maximum number of contracts persons can enter, ***taking account of the characteristics of the underlying commodity market, including patterns of production, consumption and transportation to market.***	transparent and non-discriminatory, specifying the persons to whom they apply and any exemptions, and taking account of the nature and composition of market participants and of the use they make of the contracts admitted to trading. They shall specify clear quantitative thresholds such as the maximum number of contracts persons can enter. ***1a. The limits referred in paragraph 1 shall not apply to commercial undertakings that access Regulated Markets, MTFs and/or OTFs in order to manage exposures related to their groups commercial activities or comply with regulatory obligations, considering the characteristics of the underlying commodity market, including patterns of production, consumption and transportation.***
Annex I, Section C	A revised definition of financial instruments excluding physically settled forward products is needed to avoid that physical trading is moved from today's efficient broker platforms to bilateral trading. We believe that this development would be more likely than channelling of trades which are currently OTC onto organised venues.		

	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 ð ,OTF, □ ~~and/~~or an MTF;	(6) Options, futures, swaps, and any other derivative contract relating to commodities that ***are not intended to*** be physically settled provided that they are traded on a regulated market, an OTF and/or an MTF;
	(7) Options, futures, swaps, forwards and any other derivative contracts relating to commodities, that ***can*** be physically settled not otherwise mentioned in C.6 and not being for commercial purposes, which have the characteristics of other derivative financial instruments, having regards to whether, inter alia, they are cleared and settled through recognised clearing houses or are subject to regular margin calls;	(7) Options, futures, swaps, forwards and any other derivative contracts relating to commodities, that ***are not intended to*** be physically settled, not otherwise mentioned in C.6 and not being for commercial purposes, which have the characteristics of other derivative financial instruments, having regards to whether, inter alia, they are cleared and settled through recognised clearing houses or are subject to regular margin calls;

Detailed comments on specific articles of the draft Regulation	
Article number	**Comments**
Article 24 New paragraph 2a:	The trading obligation procedure defined in MiFIR may reduce the scope recognised in EMIR. Additionally it doesn't take into consideration the rules introduced for wholesale energy markets with the Regulation 2011/1227/EC on market integrity. *Text proposed by the Commission* — *Amendment* ***2.a The obligation laid down in paragraph 1 shall not apply to wholesale energy products which are subject to appropriate monitoring by the competent prudential-supervision authorities as defined in Regulation 2011/1227/EC.***