

MiFID II TECHNICAL ISSUES

Comments on the position limits regime under Article 59 MiFID

- **Article 59(1):** It will be necessary to clarify what is meant by an "economically equivalent OTC contract", as this is not a term defined in MiFID. If this relates to OTC derivatives, Article 59(1) should say "OTC derivatives", and the term "OTC derivatives" should be defined (in line with the definition in EMIR or otherwise as appropriate). It should be clarified if this is intended to capture contracts which are not MiFID financial instruments.
- **Article 59(1):** Position limits will apply to all positions held by a person including those "held on its behalf at an aggregate group level". It is not clear what is meant by "held on its behalf at an aggregate group level" (e.g., whether this would include all aggregate positions held by any member of the group, or only positions that group members hold in custody for the relevant person). ESMA has powers to specify which group positions are required to be included, but Level 1 text should give some guidance on the scope of ESMA's powers. For example, the Level 1 text should clarify whether positions held by non-EU group members should also be counted within the position limits.
- **Article 59(2d):** This seems to indicate that if the same commodity derivative is traded on a trading venue in more than one jurisdiction, but not in significant volumes, there is no obligation for competent authorities to consult each other and each competent authority can impose different position limits in their own jurisdiction. This should be clarified in the Level 1 text.
- **Article 59(9):** Although we welcome attempts to resolve the problems of double jeopardy as a result of overlapping sanctions regimes, this wording appears to encourage competent authorities to take action against persons for breach of their own regimes as well as those of other Member States, and the way in which it is drafted could result in application of these sanctions regimes to non-EU branches of EU entities dealing with non-EU counterparties or to non-EU incorporated entities with no other connection to the EU other than that they are dealing in contracts which ESMA has determined to be economically equivalent. This should be clarified in the Level 1 text.
- Level 1 text should include transitional provisions to ensure that market participants are not required to sell down existing positions immediately upon entry into force.

Comments on the definition of financial instruments under section C(6) of Annex I to MiFID

- The carve-out for wholesale energy products as defined in Article 2(4) REMIT assumes that the reference to "derivatives" in REMIT (which is not defined) means something broader than MiFID financial instruments. If this is the case, the Commission should clarify this, and to ensure that any references to "derivatives" in other legislation specify whether these are references to derivatives which are MiFID financial instruments or references to a broader meaning of "derivatives". If this is not the case, the proposed carve-out for wholesale energy products as defined in Article 2(4) REMIT creates a circularity (as the definition of derivative financial instruments under MiFID refers to a definition of derivative under REMIT which itself refers back to the definition under MiFID).

- Transitional provision for C6 energy derivative contracts: it will be important to clarify this to avoid creating additional uncertainty:
 - Art. 99(3) appears to create an automatic time-limited exemption, but paragraph Art. 99(4) indicates that this will not be automatic but must be granted by competent authorities. It will be necessary to clarify a number of points:
 - i. Paragraph 3 should state clearly that this is an exemption that needs to be applied for, who needs to apply for it and whether the exemption is granted to each relevant counterparty entering into C6 energy derivatives (and if so, what the criteria are for obtaining the exemption) or whether the exemption will be granted on a contract by contract basis (paragraph 4 indicates that the competent authority will grant the exemption to particular C6 energy derivative contracts).
 - ii. If each relevant counterparty has to apply, who is the relevant competent authority for these purposes (along the lines of the clarification under EMIR) and how competent authorities should co-operate where both counterparties need to apply for the exemption.
 - iii. If the relevant counterparties are not required to apply, who does apply for this exemption? Or is this an exemption that competent authorities may choose to apply generally to all counterparties in their jurisdiction?
 - What happens at the end of the three-year period? Will relevant counterparties be required to submit outstanding contracts for clearing, or is any contract entered into during the three-year period exempt for its entire duration? And similarly, will relevant counterparties be required to start counting contracts entered into during the three-year period towards the clearing threshold as soon as the three-year period expires?
 - Art. 99(4) indicates that competent authorities may grant the exemption in relation to certain C6 energy derivative contracts. This needs to be clarified to give legal certainty to counterparties seeking to implement EMIR: if the UK FCA grants an exemption in relation to certain types of C6 energy derivative contracts, does this mean that only UK counterparties can rely on the transitional provisions? Or would the UK FCA's determination exempt those contracts in every EU jurisdiction? Can competent authorities withdraw their exemptions, with the result that a particular type of contract may become a financial instrument without warning? Can competent authorities designate a type of contract as exempt at any point during the three-year period, with the result that some contracts may cease to be financial instruments without warning? In the interests of legal certainty, the scope of the "C6 energy derivative contracts" that benefit from the three-year transitional period should be defined under MiFID and competent authorities should not have the power to expand or reduce the scope of this definition. If this is intended to be an exemption that counterparties must apply for, the exemption should be granted in relation to all C6 energy derivative contracts (as defined in MiFID) entered into by counterparties that meet the criteria for benefiting from the exemption.