

## **Q&As MiFID II commodity derivatives**

**Disclaimer:** The purpose of this publication is to assist you with your preparations for MiFID II implementation. Nothing in the below content is intended to direct or encourage you towards a specific course of action. You should seek your own professional advice on the application of MiFID II requirements to your business. Further, no comment is made on any matter that is presently the subject of public consultation. This publication does however reflect the content of recently published Policy Statement 17/14 (which includes the finalised version of rules originally published in Policy Statement 17/5). This document is published as a working draft, and may be subject to further amendment going forward.

### **Ancillary activities notification**

**Q1: How should an entity considering a notification or application approach the data published by ESMA which does not include 2017 figures?**

A: Entities should refer to the PERG guidance on the ancillary activities notification (AAN) published in PS17/14. Entities should also be mindful of ESMA's statement on the market size data and its inherent limitations. Following an assessment of the figures, if an entity finds that it is significantly below the relevant thresholds, it could reasonably assume that it would pass the overall market threshold test in RTS 20. Subject to also satisfying the main business threshold test in RTS 20 it could submit an AAN form. ESMA's Opinion containing the market size data can be found [here](#).

Entities have the ongoing responsibility to monitor for amendments to the data, and also to reassess when the 2017 (and remainder of 2016) data becomes available.

**Q2: Who has responsibility to make the annual notification to the FCA when making use of the ancillary activity exemption?**

A: Any natural or legal person that deals on own account or provides investment services in commodity derivatives as a regular occupation or business on a professional basis and who makes use of the ancillary activity exemption has to notify annually their relevant competent authority that they make use of this exemption.

### **Position limits**

**Q3: When will the position limits be published?**

A: The FCA will publish the position limits where it is setting a bespoke limit for a commodity derivative contract in Q4 2017.

**Q4: Will there be a different position limit for options and futures? If so, how should options be converted into futures for the application of position limits?**

A: No, separate limits will not be set for futures and options on a commodity derivative. Please refer to the published ESMA Q&A for further details.

**Q5: Will you be publishing a list of EEOTC contracts?**

A: No. It is the responsibility of the investment firm who enters into an OTC transaction to determine whether it is an EEOTC contract in accordance with MIFID II

## **Position limit exemption applications**

### **Q6: What approach is the FCA taking for position limit exemptions**

A: The exemption will be an uncapped exemption based on an assessment of the application. The FCA will monitor reported positions against the information provided in the application form. If there is a significant change in the nature or value of the non-financial entity's commercial or trading activities, in the circumstances described in article 8(4) RTS 21, it is required that the entity should submit a new application.

### **Q7: How should an entity approach the position limit exemption application if it is uncertain if it passes the Ancillary Activity Test?**

A: An entity can make a position limit exemption application to us provided it reasonably believes it satisfies the definition of an NFE. One way an entity could qualify as an NFE, is through making use of the ancillary activity exemption in article 2(1)(j) MiFID II.

Should more accurate data (e.g. in the form of updated market size figures from ESMA) come to light, an entity should reconsider whether its status as an NFE and any previously submitted position limit exemption applications remain valid.

Firms who find that they are relatively close to the market thresholds based on ESMA's published data can in principle also submit a position limit exemption application to the FCA although they have the ongoing responsibility to monitor for amendments to the data, and also to reassess when the 2017 data becomes available.

### **Q8: What is the latest date I can apply to ensure I know the outcome of my application before the 3<sup>rd</sup> of January 2018?**

A: The FCA expects entities to apply by the 1<sup>st</sup> of December at the very latest. Earlier applications are encouraged. After the implementation of MiFID2, the FCA has 21 calendar days to approve or reject a complete application.

### **Q9: Who should I contact if I have a query regarding an exemption application?**

A: Entities can email [PLexemptions@fca.org.uk](mailto:PLexemptions@fca.org.uk)

### **Q10: When can I apply for an exemption?**

A: The exemptions application gateway will open at the beginning of October 2017.

### **Q11: How are firms expected to know whether an NFE client has a position limits exemption?**

A: Firms are not required to monitor the position limit compliance of their clients. Compliance is the responsibility of the position holder. So there is no expectation that a firm (such as a broker) should know, or need to know, the exemptions granted to any individual person.

### **Q12: Will position limit exemptions granted be listed publicly?**

A: No. The approval of a position limit exemption is a matter between FCA and the applicant.

**Q13: How will the position limits exemption be specified – e.g. on a product basis or on a contract by contract for a product basis?**

A: It should be applied for and will be approved on a commodity derivative contract basis. MiFID II requires that position limits are set for each commodity derivative.

**Q14: Does the position limit exemption apply to the client's whole position or only to trades entered into after the granting of the application (thereby requiring position reporting net pre-exemption granted and after exemption granted?)**

A: The position limit exemption applies to the whole position, regardless of when particular positions were entered into. The approval of a position limit exemption does not change the reporting which is required under Art.58 of MiFID II and ITS 4 in any way. Firms should not apply any exemption granted in the reporting of the positions of a client.

**Q15: Where a client has a position (e.g. long on an ETD) before the position limit exemption was granted and executes short trades in the position after the exemption is granted, are we expected to report the total of the long position prior to the exemption being granted as not exempt and the net short position as exempt, or just the total net position as exempt?**

A: See question 14.

**Q16: If a client receives position limit exemption, do we have to cancel previous reports and resubmit with the risk reducing flag set to yes (on the assumption the position limit exemption applies to the total net client position regardless of when trades were entered into).**

A: No, see question 14. The risk-reducing flag refers to the purpose for which the position is held, and not whether or not a position limit exemption has been approved for that person.

### **Reporting**

**Q17: Can a firm delegate its position reporting obligations to third party technology providers?**

A: A firm can delegate the operational function of submitting the reports to a third party technology provider but the responsibility remains with the firm so the firm subject to the reporting requirement must complete a MDP on-boarding application and pay the relevant connection fee. Please see MAR 10.4.11 G, as published in PS 17-14, for further detail.

**Q18: Do securitised derivatives below the threshold of 2.5million need to be reported?**

A: No as clarified by ESMA Q&A they do not need to be reported.

**Q19: Do Emission Allowances need to be reported?**

A: Emission allowances classified as C(11) financial instruments for the purposes of MiFID II are explicitly required to be reported, but they will not have a position limit.

**Q20: When do position limits apply?**

A: Position limits apply from the 3<sup>rd</sup> of January 2018 and will apply at all times thereafter.

**Q21: Would you expect investment firms when calculating their positions to be reported to the FCA to report the net position across a contract that is traded on a trading venue and contracts that are economically equivalent to that venue contract, or would you expect to see the on venue contract and any economically equivalent contracts to be reported separately?**

A: They should be reported separately.

**Q22: Does position reporting and position management controls apply to inflation products?**

A: ESMA Q&A has clarified that position limits will not be set on derivatives where the underlying is not a commodity. This means that no position limits will be set for inflation products. Although inflation derivatives will not have specific position limits, the requirements on trading venues under other parts of Art.57 and Art.58 of MiFID II still apply.

**Q23: How does a venue who does not currently have visibility of the member or participants' positions meet its reporting obligations?**

A: The nature of the reporting arrangements of the member or participant are a contractual matter between them and the venue; the trading venue must be able to meet its obligations to FCA under Art.58(1)(b). Additionally, MiFID II sets an explicit requirement in Art.57(8)(a) for all Regulated Markets, MTFs and OTFs to monitor the open interest positions of persons.

**Q24: What is the definition of a lot for energy products?**

A: Please refer to the ESMA Q&A (Q2 'What is the definition of a lot for energy products?').

**Q25: Should positions with different maturities within the non-spot month period be netted to apply the other months' limits?**

A: Yes. All separate positions in maturities across the curve excluding those positions in the spot month for that commodity derivative should be summed or netted.

**Q26: Recent ESMA Q&A clarifies that investment firms must report the position of its non-investment firm client which is its 'end-client' together with the positions that such 'end-client' holds on behalf of third parties. ESMA further encourages investment firms to report the position of its non-investment firm 'end-client' separately from any positions that end-client holds on behalf of third party entities. ESMA notes this may avoid erroneous reporting of breaches of position limits by the end-client.**

**(a) Does the FCA agree with ESMA Q&A Section 4 Q 2?**

A: Yes, FCA is a member of the ESMA CDTF which agreed these Q&As.

**(b) As the position aggregation at the level of the end-client would not allow for the identification of further underlying position holders, does ESMA's description of such**

**position aggregation therefore override ESMA's statement in the Q&A Section 4 Q 10 that 'the requirement to identify clients and clients of clients until the end client in position reports cannot be waived'?**

A: No, the end-client is a different concept to that of any ultimate position holders who may not be an end-client according to the definitions within MiFID II. Should there be aggregation at an end-client level which is initially unidentified, it may come to light during in depth monitoring.

**Q27: Although there is an ability to cancel an existing report and send an amended report, if we identify that a historical report is incorrect while the current T+1 report is correct, do we have to cancel the historical report and reproduce it with the correct values? If so, how far in the past does this apply?**

A: Yes, MDP will accept corrections for up to 5 years after the trading day to which the report relates.

**Q28: For the purposes of cancel and amends, do we cancel and replace the entire day's report or just the lines in the report that are in error?**

A: MDP will not accept a report without all the relevant fields completed. Any revising report should contain data in all the relevant fields including the amended data – our system will pick up the changes.

If the record was submitted in error then the submitting entity should resend the report with a Report Status of CANC in order to cancel the report.

If a report needs to be amended and the updates relate to fields that make up the unique key (namely, report reference number, date of the trading day, venue product code, and position holder ID) for a position report, then the entity should send a report with a Report Status of CANC in order to cancel the initial report. Provided the cancellation is accepted, the entity can then submit the correct version of the record with a Report Status of NEW.

If a report needs to be amended and the amendments do not affect the data that was originally reported in any of the fields that make up the unique key for a position report, then the entity should resend the report with the relevant corrections and a Report Status of AMND.

For further details please refer to the FCA reporting instructions [here](#).

**Q29: Where trades are executed in a contract that would be reported in Other Months, is the position arising to be reported in the Spot Month category if it is still held when that contract enters the spot month?**

A: Yes. The Spot/Other month categorisation for position reporting is driven by the date of expiry of the position, not the execution date.

**Q30: If a position is contained solely of decomposed index trades, what value are you expecting in the position quantity field?**

A: FCA is not expecting indices to be decomposed into separate positions. See ESMA Q&A PL10.

**Q31: Is the Delta Equivalent quantity required for options over futures contracts?**

A: Yes, see ESMA Q&A PL9.

**Q32: Are index positions decomposed to an ETD to be reported as an ETD or EEOTC position?**

A: Neither. Index positions should not be decomposed. See question 30.

**Q33: What is the scope for both position limits and reporting for commodity derivatives traded OTC which are not considered EEOTC**

A: Article 57 and 58 of MiFID II apply to commodity derivatives traded on a trading venue and any EEOTC contracts.

**Q34: Position reporting: what constitutes one record? Net position per position holder per ISIN (i.e. option series) or per venue product code? The latter contradicts to ITS4, as field 14 cannot be filled correctly if futures and options are grouped**

A: Futures and options should be reported separately which is reflected in the position report field 'instrument name'. The position limit applies per Venue Product Code so the different instrument types will be aggregated by the FCA in its calculation to determine whether a position limit has been breached.