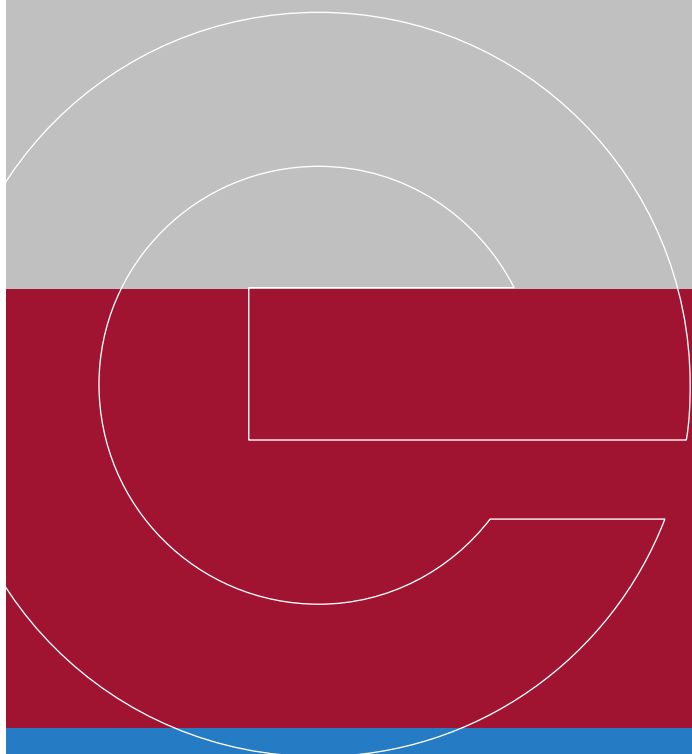


Position Paper

Response of the German Association of Energy and Water Industries (BDEW)
on CESR's/CEBS's technical advice to the European Commission on the
review of commodities business

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BDEW's answers to the Consultation Paper

The German Association of Energy and Water Industries (BDEW) represents 1,800 members of the electricity, gas and water industry. In the energy sector, we represent companies active in generation, trading, transmission, distribution and retail.

We welcome the opportunity to comment on the CESR/CEBS Consultation Paper. Before answering the specific questions of the Consultation Paper, we want to highlight some important features of the commodity markets and in particular the energy markets which clearly differentiate them from other financial markets. These specificities should be carefully considered in the current review process and, in our view, these specificities necessitate that energy companies in general have to be subject to a different regulatory framework than financial institutions do. The goal should be to establish a reasonable financial regulation for energy trading which does not impede the development of the European energy markets.

Energy markets are subject to specific energy regulation. Wholesale energy markets are already subject to various other energy-related legislation. The Directive 2003/54/EC and Regulation 1228/2003/EC for electricity and Directive 2003/55/EC and Regulation 1775/2005/EC for gas in particular set the legal framework for the internal energy market (certainly the legal provisions for the Greenhouse Gas Emissions Trading Scheme as well as the currently proposed "Green package" have further significant impact on the energy market). In reference to these legal foundations a harmonised approach of implementation and supervision is vital to avoid distortions for cross-border energy wholesale trading.

Thus, the energy markets shall predominantly be governed by this set of energy regulations (and the respective energy regulators) and not in addition by financial market regulation. Consequently, probably the most important challenge of the current EU legislative framework is to define the appropriate borderline between financial market regulation and the regulation of the physical energy markets and – if there is an interface – to find appropriate measures to deal with it.

No involvement of non-professionals in energy markets. Besides the protection of the stability of financial markets the main purpose of financial

market regulation is investor protection. However, although this is a vital aspect in the financial business, this issue is less relevant in the energy sector as it is a purely professional market. Energy trading markets have a specific set of characteristics compared to traditional financial markets. While financial market regulation predominantly addresses market and credit risks as well as the operational risks of the traditional financial services market, it does not specifically consider the innate conditions of the energy wholesale markets. While on financial markets the flow of capital is predominant, the main objective in European energy markets is the production and supply of energy. Both energy trading (including energy derivatives trading) as well as the customers they serve are of wholesale nature. Thus, the relevant risks presented by such wholesale markets (security of supply and robust prices for end-customers) are significantly different to those present in financial markets (systemic risk and investor protection). Furthermore, e. g. electricity markets are, more or less, invested in generation and transmission assets. Such assets serve as underpinning for possible remaining risks and there is no necessity to provide additional core capital.

Energy companies use derivatives for risk management and hedging.

Trading by energy companies is mostly done on own account for risk management and hedging purposes. While the production of the generation companies is sold to the market, supply companies without generation facilities need to purchase electricity on the market to supply their customers. This is also true within integrated companies for their generation and supply entities where the trading entity is buying and selling from/to the market. To mitigate the arising price and volume risks, trading of energy on own account on energy wholesale markets is, most commonly, used as risk management and hedging tool. This does per se not lead to any risks for third parties, particularly as exchange based trading is cleared through a central counterparty and bilateral trading is mostly done based on master agreements which foresee for clear rules for reducing credit risks.

The financial systemic risk of energy trading is not comparable to classic financial markets. Activities in energy trading do not imply the same financial systemic risk as activities in the classic financial markets and hence should be treated differently in respect to CRD requirements. Due to differences in the internal organisation as well as market and

customer structures, the market price risks and counter-party risks as well as the operational risks caused by energy trading companies vary fundamentally from those that may be triggered by companies in the classical financial sector. The energy trading market is a purely professional market with only sophisticated participants. Moreover, the majority of energy related contracts are concluded in order to physically deliver energy.

The other main focus of the financial market regulations – besides investor protection – is to limit the systemic financial risks resulting from the instability of financial institutions, investment companies and banks in the financial market. In comparison to the failure of one of those classic participants in the financial market, the insolvency of a market player in the energy market cannot lead to a disturbance of the capital market itself. A prime example is the insolvency of the energy trader ENRON that did not lead to a major disturbance in the financial markets. The methods of risk and credit management used in energy trading have proved that they are adequate to guarantee the functionality of the energy capital market. Notably, insolvency will not affect generation capacity as these capacities will most likely not disappear from the market, but rather continue to be used, possibly under new ownership. Thus, the energy market holds a lower level of systemic risk for the financial market than the classical financial market.

The different company, client and product structure in energy markets lead to lower credit risks. Credit risks in the energy trading industry are considerably lower as in the pure financial sector. A major difference between energy markets and financial markets is based on the fact that in energy markets the products are physically delivered. In power and gas markets a (constant) load is transferred through a period of time. In matters of capital structure, organisation and core business, energy trading companies vary significantly from companies in the financial sector. Customers of energy trading companies comprise mostly distributors, municipalities, large industrial companies and to a lesser extent members of the classical financial sector. The transactions conducted on the energy market mostly serve to supply end-customers or distributors. Moreover, energy trading is a vital means for an effective management of the generation capacities and provides the important measures for risk management activities of energy suppliers, energy

producers and energy consumers. Essentially, energy trading is based upon the physical exchange of power, gas and coal with the purpose of ensuring security of supply and the hedging of risks. In contrast, the majority of the classical financial sector comprises bank and investment-related activities, such as traditional banking and investment services.

Having set out these general features of the energy markets and energy companies, we will in the following answer the specific questions of the Consultation Paper, referring where appropriate to the general remarks above.

Questions

- 1. In practice, what proportion and/or amount of OTC *commodity [derivative]* transactions are financial instruments falling within the *MiFID* and what proportion are spot? (a breakdown in terms of the underlying would be helpful)
(p. 12)**

We assume that the intention of this question is a differentiation between commodity transactions which are financial instruments and commodity transactions which are spot transactions (cf. para 33 of the consultation paper).

As the definition of financial instruments in the MiFID is rather extensive, we reckon that with regard to energy commodities a large portion of OTC forward transactions may fall under the definition of financial instruments according to the MiFID definition, without being able to provide concrete figures.

- 2. Do you agree that the level of direct participation by unsophisticated investors is mainly limited to corporate clients such as producers or wholesale distributors (with a lack of experience and knowledge in derivative markets but not in trading in physical *commodity markets*), that participation by**

**private clients is very low, and that most other participants in commodity derivatives markets are sophisticated firms?
(p. 21)**

The consultation paper sets out that in commodity derivative markets there is almost a complete absence of direct investment by unsophisticated individuals and private clients. We fully support this observation. In particular, customers of energy trading companies comprise mostly distributors, municipalities, large industrial companies and members of the classical financial sector, which are considered as sophisticated investors. Consequently, as there are almost no unsophisticated investors, the issue of investor protection in energy derivative markets is not as relevant as in the traditional financial sector.

**3. What informational advantages persist in commodity derivatives markets, and in particular to what extent do those also active in the underlying physical market have informational advantages?
(p. 21)**

As a general point, any alleged informational asymmetries should be addressed in the course of discussion regarding transparency in the energy market and not by financial markets regulation.

As stated in the consultation paper (para. 65), informational asymmetries between sophisticated firms are in general relatively small. This also applies to the energy derivatives markets. In our view, there are also no significant informational advantages of those companies which are also active in the underlying physical market. The various transparency initiatives mentioned below also ensure that informational asymmetries in the energy markets are low.

Besides information already required by law, market related information can be obtained through various additional channels. Generally, transparency on energy exchanges is ensured by the exchange itself, where market players can see e.g. the traded

volumes, bid and ask curves, number of players and clearing prices. Regarding OTC-trading the broker screens in use in modern trading rooms allow for market players to see e.g. the bid and ask prices and the traded volumes (including open interest). Additionally, a range of further detailed ex-post information is provided by brokers and information providers. There are several independent information service providers (e.g. Platts, Bloomberg, Reuters) that offer a range of market relevant data and information. Such information include for example market related news, analyses, weather data, exchange/ benchmark prices, or data on generation.

Additionally, there have been various transparency initiatives launched in the context of the Regional Initiatives (e.g. ETSOVista) as well as on a national basis. To mention is for example the voluntary initiative to publish generation-related data via the website of the EEX which provide for information on status and actual use of generation units. BDEW, in cooperation with other associations and the German ministry of economy, has started a transparency initiative which shall ensure the central publication of relevant data at an EEX platform. Other energy exchanges also publish a range of market relevant data. BDEW fully supports clear and harmonised rules for market transparency throughout the European Union.

In this context we would like to point out, that the recent Sector Inquiry of the Commission, although describing a number of problems affecting wholesale markets (such as vertical integration, lack of integration of national markets), did not indicate any problem regarding commodity and commodity derivatives trading and did not propose additional measures concerning transparency or supervision of energy commodity markets.

**4. Do information asymmetries in *commodity derivatives markets* lead to mis-selling concerns, or to other concerns about potential client detriment?
(p. 21)**

We do not see any information asymmetries in energy derivatives markets (s. also answer to question 3).

5. **Do you have any transparency-related concerns relating to the trading of non-electricity and gas *derivatives*? If so, in which markets and why?**
(p. 23)

Following our answer to question 3, we also do not see any transparency-related concern with regard to other energy-related derivatives (e.g. EUAs).

6. **Do you have evidence of informational asymmetries in *commodity derivatives markets* in relation to market abuse?**
(p. 25)

As set out in our answer to question 3 above, we do not see that there are informational asymmetries in energy derivatives markets and, therefore, do not see the potential for market abuse. In addition, any pertinent concerns in this respect are taken care by the transparency initiatives mentioned above and are subject to the current CESR/ERGEG consultation on market abuse issues.

7. **Please provide any information you may have on the levels of lending and trading exposures between *specialist commodity derivative firms* and *institutions*.**
(p. 27)

From the perspective of specialist energy derivative firms, there is an increasing level of trading activities between specialist commodity derivative firms and institutions following the rising participation of financial institutions in the energy derivatives markets.

With regard to trading exposures, however, it should be noted that exchange and platform based trading is usually cleared through a central counterparty. Bilateral trading is mostly done based on master agreements which have clear rules for reducing credit risks. To an increasing extent, bilateral trading is cleared through central clearing houses and thus counterparty credit risks are reduced.

In energy trading, debt guarantees or comfort letters by holding companies are widely used as collateral. Thus, the lending exposures are limited.

**8. What level of risk do *specialist commodity derivative firms* pose to the financial system?
(p. 29)**

The consultation paper sets out that so far there have been no cases in which interconnections between specialist commodity derivative firms and other financial institutions have led to significant financial instability. It concludes that the systemic risks generated by specialist commodity derivative firms are relatively low. We fully agree with this observation.

As discussed in the general remarks above, activities in energy trading do not imply the same financial systemic risk as activities in the classic financial markets and hence should be treated differently in respect to CAD. The functioning of the energy-related capital market is therefore much less affected by trading-related risks. Due to differences in the internal organisation as well as market and customer structures, the market price risks and counter-party risks as well as the operational risks caused by energy trading companies, vary fundamentally from those triggered by financial institutions. The majority of energy related contracts are concluded in order to physically deliver energy. The main focus of the financial market regulations is to limit the systemic financial risks stemming from the activity of financial institutions, investment companies and banks in the financial market. In comparison to the failure of a classical participant in the financial market, the insolvency of a market player in the energy market cannot lead to a disturbance of the capital market itself. As described above, the insolvency of Enron did not lead to a major disturbance in the capital/financial markets. The insolvency also had only a short-term impact on energy wholesale prices.

The methods of risk and credit management used in energy trading have proven that they are adequate to guarantee the functionality of

the (energy) capital market. Thus, the energy market holds a lower level of systemic risk than the financial market; and notably, insolvency will not affect generation capacity as these capacities will most likely not disappear from the market, but rather continue to be used, possibly under new ownership.

- 9. To what extent does the level of systemic financial risk posed by *specialist commodity derivative firms* differ from that generated by banks and *ISD investment firms*?
(p. 30)**

We refer to our answer to question 8.

- 10. Do the risks generated by energy-only investment firms differ materially from those posed by investment firms engaging in other commodity derivative activities/services? If so, how do they differ?
(p. 30)**

In our opinion, the differences between the risks connected with energy commodity and the risks connected with other commodity derivative activities/services are considerably lower than the differences between the risks posed by institutions. Therefore, we think that one regulatory regime suited for all commodity derivative activities would be appropriate.

However, we disagree with the conclusion in para. 104 of the consultation paper that the non-storability does not lower the prudential and systemic risks for energy-only firms and rather believe that the risks connected to the failure of an electricity firm are consequently lower.

- 11. Do you have any transparency-related concerns relating to the trading of non-energy commodity derivatives, and, if so, in which markets, what are the concerns, and what solutions could be applied?
(p. 33)**

n/a

- 12. Do you believe that for non-electricity and gas derivatives contracts, the transaction reporting requirements in the MiFID support market regulation? If so, can you explain why you think they do?
(p. 35)**

n/a

- 13. Do you have any evidence on potential problems, and if so, on the scale of these problems, that are posed by current client categorisation rules?
(p. 36)**

n/a

- 14. Do you have any evidence that regulation according to the main business of the group may cause competitive distortions?
(p. 37)**

No, we do not believe that the differences in regulatory treatment between categories of firms that provide investment services in relation to commodity and exotic derivatives and across Member States have given rise to a regulatory failure. Hence, we do not see a competitive distortion which could be of significant policy concern, particularly when considering the energy industry.

The specific exemptions for commodity firms in both MiFID and CAD are important to recognise the specific nature of energy and energy

trading markets. Due to the hedging nature of energy and energy derivative markets, the risks are related to security of supply and end user price. And these regulatory risks are substantially different to those common in financial markets (i.e. financial systemic risk). Therefore, the commodity-specific exemptions are very reasonable, as they help to avert much bigger competitive distortions for energy firms which would arise if rules, which are aimed to meet risks of the financial market, were applied to firms that do not contribute to such risks. Otherwise, particularly small and medium sized companies that are active in energy trading market may be forced out of the market (or may never consider to enter), which in turn may lead to results that are in contrary to the aim to establish a competitive European energy market and thus are contrary to the objectives of the Energy Directives.

We think that a difference should be made between the provision of investment services by investment firms and by energy companies. Financial market regulation predominantly addresses market and credit risks as well as the operational risks of the traditional financial services market, thereby not considering the innate conditions of the commodity trading business of the energy companies. Due to differences in the internal organisation as well as market and customer structures, the market price risks and counter-party risks as well as the operational risks caused by energy trading companies, vary fundamentally from those triggered by banks, financial institutions or investment companies in the classical financial sector.

Therefore, a distinction between institutions and energy trading companies seems to be adequate.

- 15. Do you agree that full application of *CRD* capital requirements to *specialist commodity derivative firms* is likely to impose a regulatory burden that is misaligned with their potential systemic impact?
(p. 40)**

Yes, we fully agree. The structure of the energy markets is very specific: Wholesale trading in electricity companies is mainly based

on own account trading and conducted for hedging purposes, while the generation segment of the industry is very capital intensive. Subjecting the energy trading business to the full requirements of CAD constitute a disproportionately large impediment, which may further prevent the market from developing. Therefore, the current capital regulation should not apply on a one-to-one basis to energy derivatives firms and their energy derivatives business. Energy companies do not create the same risks nor do they have the same capital structure as investment firms. Thus, the application of a specific commodity-related prudential regulation would be an adequate treatment of different situations in different market segments.

Regarding the capital structure there are also differences between energy companies and pure investment firms. The former are much less leveraged than investment firms; having in many cases invested their main capital into physical assets, they have a different client base (only wholesale customers and none or insignificant retail customers) and they face different risks (no systemic financial risk). Hence an undifferentiated application of capital adequacy and core capital etc. would constitute a disproportionately huge impediment, which may further prevent the market from developing as it may hamper liquidity (crowding out of market participants and possible relocation of business outside the EU), which in turn will obstruct the liberalisation of the European energy markets.

Therefore, we opt for a procedure, which allows for developing a commodity-specific prudential scheme based on sufficient experience. Particularly in relation to the capital regime we see the need for a more flexible approach of prudential regulation accounting for the specificities of the energy business. This system should be based on best risk management principles, internal processes and risk bearing capacity (sufficient financial resources) rather than regulatory capital.

- 16. Do you believe that full application of *CRD* large exposure requirements to *specialist commodity derivative firms* is likely to impose a regulatory burden that is misaligned with their**

**business and their business and their potential systemic impact?
(p. 40)**

Yes, we fully agree that the full application of the CRD large exposure regime to specialist commodity derivatives firms would impose unjustified regulatory burden on the business of these firms. It is common practice that energy is supplied throughout the entire month with the metering of the actual usage and the issuing of the bill at the end of the month. Further, the supply company then usually allows for a deferred payment (i.e. a specific time after issuing the bill). The established practice of delivery and payment modalities are one month plus 20 days post delivery. This is mainly due to the fact that the energy supplier will only at the end of the month know the actual delivered quantity and commonly grants a term of payment of 20 days.

This could lead to the fact that the upper limits for large exposures are quickly reached and exceeded. As a consequence, the capital requirements to cover large exposures would also have to be met. In other words, if an energy supplier is also active in "MiFID-licensed" trading, the usual commercial operations like supply of electricity, gas or heat would cause an inappropriate additional need for capital adequacy due to the capital requirements for Large Exposures. However, the commercial customs and established procedures can only be changed with major efforts and cost, while alternatively additional equity will be difficult or almost impossible to obtain. Moreover, energy companies often pool power purchasing and selling activities in a group or affiliated company to purchase and sell volumes. Thus, large and multimillion exposures limits will be easily reached and even exceeded. Such companies would then be forced to raise considerable additional funds to satisfy the resulting capital adequacy requirements, which will be a large impediment for their future business activities.

This would constitute a barrier to market entry and may seriously impede the future development of liquid energy trading markets in the EU.

**17. Do you believe there is a potential for regulatory arbitrage? If so, can you provide evidence?
(p. 42)**

Although, we see the potential for regulatory arbitrage, we do not consider it as the main reason for regulatory failure. In fact, we believe that national over-regulation of the wholesale trading activities of commodity firms (“gold-plating”) is the driving force to change business activities towards Member States where the regulatory frameworks are more open to cost-effective participation in commodities markets.

Currently, regarding MiFID and CAD, Member States are free to extend the scope of the MiFID also to non-MiFID business as they may choose not to implement the MiFID exemptions and to extend the current definition of commodity derivatives. This may cause significant regulatory uncertainties, which can only be avoided if the scope of the regulations is made equivalent across all Member States and the exemptions and definitions of MiFID are implemented in a reliable and firm manner by the Member States (full harmonisation on a one-to-one basis). This means, the MiFID definitions and exemptions shall be binding for all Member States without allowing for super-equivalent national implementation. Differences in regulatory treatment between Member States cause immense uncertainties and should be avoided; they may force energy trading companies to establish separate regulated trading affiliates to avoid regulatory uncertainties resulting from trading activities in other Member States, when in their home jurisdiction they would be exempt. This will clearly impede small participants from engaging in cross-national trading activities as they may not afford the expenses for the establishment of separate regulated trading affiliates to avoid such uncertainties. This would, in turn, constitute a barrier to market entry and thus lead to competitive distortions on the cross-national level and impair the free movement of services between Member States.

We have observed that the implementation process of the specific exemptions across the Member States has not been conducted in a harmonised way. MiFID exemptions have only partly been

implemented or not implemented at all; there are differing interpretations on the exact application of the exemptions; even if the MiFID exemption have been implemented there may be a differing approach to the issue of also applying the relevant CAD exemptions.

As an example where specific MiFID provision have only partly been implemented, we like to refer to the transformation of exemption 2 (1) i MiFID into German law, which makes the exemption not only dependent on financial services being carried out for customers of the main business segment. Additionally, it is also required that the financial services are correlated to the main activity (see § 2.a.I.9.c WpHG and § 2.VI.11.c KWG). This precondition severely limits the application of the exemption and, therefore, impedes competition.

- 18. Do you believe that the application of the *MiFID* organisational requirements support the intended aims of market regulation when applied to *specialist commodity derivatives firms*, or *commodity derivatives business*? If not, what aspects of the organisational requirements do you believe do not support the aims of market regulation when applied to such firms and why? (p. 44)**

We assume that the intended aims of the market regulation are investor protection and systemic stability of the financial markets. With regard to specialist commodity derivatives firms, the organisational requirements serve self protection of the firms concerned. However, we think that investor protection and systemic stability are not put at risk by the activities in the specialist commodity derivatives sector (cf. our answers to questions 8, and 10) Therefore there are no organisational requirements that could provide additional benefit to the intended aims of market regulation.

- 19. Do you believe that there is a case for changing the client categorisation regime as it applies to *commodity derivatives business*? If so, do you have any evidence on the scale of the**

**problem or potential problem posed by existing rules?
(p. 46)**

As set out in our answer to question 2, the energy derivatives business is characterised by being almost completely done by sophisticated market participants.

In particular with regard to the German energy market, it has to be noted that it is very heterogeneous in nature, with many smaller firms (Stadtwerke) that are well experienced but may not qualify as professionals under MiFID. As this may lead to additional regulatory burden for energy traders with a MiFID license, they may be hesitant to do business with those smaller firms. Also, many of these potential small firm clients are producers or consumers of considerable amounts of the underlying commodity. For those it would become more difficult to effectively hedge their physical positions, because counterparts (with MiFID license) might not do business with them, because of the regulatory burdens involved, or at higher cost.

Therefore current client categorisation rules may hinder the further development of the energy market (e.g. increasing liquidity). Generally, any client categorisation must be challenged by its need with respect to the aim of investor protection.

- 20. Do you believe that the conduct of business rules in the *MIFID* effectively support the aims of regulation with respect of *commodity derivatives business*? If not, can you explain why and in what respects, and whether your response is contingent upon the client categorisation definitions applied to *commodity derivatives business*?
(p. 46)**

With respect to conduct of business rules we would like to refer to our answer to question 18.

- 21. Do each of the following elements of the criteria for determining which commodity derivatives contracts are financial instruments offer sufficient clarity to market participants to understand where the boundaries of the *MiFID* lie?**
- a. the phrase “...that must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event)”;**
 - b. the phrase “traded on a regulated market and/or MTF”**
 - c. the definition of a spot contract in Article 38 (2) of the *MiFID* implementing regulation;**
 - d. the criteria in articles 38(1) (a), (b) and (c);**
 - e. the definition of a commodity in Article 2 of the *MiFID* implementing regulation; and**
 - f. the list of underlyings of exotic derivatives mentioned in Section C(10) of Annex I to the *MiFID* and Article 39 of the *MiFID* implementing regulation.**
(p. 51f)

Although we recognize the complexity of the definitions and criteria above, we believe that there is room for improvement with regard to the clarity of various elements.

In particular, the scope of “freight rates” in Section C (10) of Annex I to the MiFID could be clarified.

Generally, any definition of financial instrument must be measured by the necessity of it being subject to financial regulation for the aims of investor protection or stability of the financial market.

- 22. Do you have any evidence of physically-settled commodity OTC contracts being written in a way that removes them from the definition of financial instruments?**
(p. 52)

n/a

- 23. Do you believe there are sufficient similarities between different *commodity derivatives markets* to make it inappropriate to differentiate the regulatory regime on the basis of the underlying being traded?
(p. 52f)**

We refer to our answer to question 10.

- 24. If the capital treatment of *specialist commodity derivative firms* is resolved, do you think there is still a case for retaining both of the exemptions in Articles 2(1) (i) and (k)? If not, how do you think the exemptions should be modified or eliminated? If the exemptions in Articles 2(1) (i) and (k) were eliminated, what effect do you think this would have on *commodity derivatives markets*?
(p. 60)**

We think that independently of the question how the capital treatment of specialist commodity derivative firms is resolved; there is a strong case for maintaining both of the exemptions in Articles 2(1) (i) and (k). The regulatory burdens connected with the removal of the exemptions would be highly disproportionate compared to the negligible systemic risks posed by energy companies. The effect would be to encourage regulatory arbitrage and increase costs, especially for small players.

Therefore we strongly favour maintaining both of the exemptions in Articles 2(1) (i) and (k). However, if this approach were not followed and if it were decided to modify the current exemptions, we would propose to “harmonise” the second limb of Article 2(1) (i) and Article 2(1) (k); i.e. it should be replaced by a single exemption covering persons (other than operators of an MTF or of a regulated market) whose business consists of dealing on own account with professional investors in relation to commodities and commodity derivatives or other non-financial derivatives contracts covered by MiFID (under points 5, 6, 7, 9 and 10 Section C, Annex I). This

exemption should apply to such an entity's activities when dealing on own account in those derivatives contracts with professional investors, including when it is dealing on own account by executing client orders. Additionally, the exemption should be also available in relation to investment advice with respect to commodity derivatives. The new exemption should be structured in a way that is clear and less open to misinterpretation.

Additionally we would like to point out some issues coming with the exemptions which may be considered in the consultation process:

The reference of the current exemption Article 2(1) (i) to customers of the main business activity creates competitive distortions. Energy trading companies without licensed affiliates cannot provide investment services in commodity derivatives for businesses, which are not customers of their physical energy products. At the same time companies which can afford a licensed affiliate can offer energy related financial services to all businesses, whether those are customers of their physical products or not. This is a severe impediment, which is not in line with the intention of the exemption in Article 2(1) (i) and the intention to create increasing competition in the energy market.

To avoid the aforementioned competitive distortion we suggest linking this exemption MiFID not to customers of the main business activity but to commodities of the main business activity (i.e. energy and energy related commodities). The rationale behind this is, that the different risk structure of energy companies and investment firms, which originally allowed for the introduction of the exemption, does not originate from the customer structure but from the product structure of the main business activity (i.e. supply of energy).

Generally, we strongly recommend to make the relevant existing or any proposed exemptions (particularly Article 2(1) (i) and 2(1) (k)) mandatory. As stated before, it is not appropriate to leave it to the Member States' discretion to impose regulations on companies that are originally excluded from the scope of MiFID. We strongly reject the implementation of any super equivalent requirements or "gold-plating" by Member States.

Besides investor protection and securing the financial market, MiFID is aimed to provide the framework for the harmonisation of the regulatory framework of the European financial markets in order to create a Europe-wide level-playing field. Electricity trading is a European business. Therefore, any unequal implementation of MiFID by Member States will create distortions for cross-border electricity trading which in turn will impede the Internal European Market for electricity and gas. Hence, the Commission should prevent any uneven or super equivalent implementation of the financial regulatory framework. To achieve this, the Commission could remove the discretion of the Member States in relation to the implementation of the exemptions – e.g. by transferring MiFID's exemptions to a MiFID Regulation – and to make the implementation of the exemptions in Article 2(1) mandatory. This would ensure a European-wide one-to-one implementation avoiding specific domestic special regulation.

- 25. Do you believe based on the above analysis that the application of the *CRD* large exposures regime to specialist *commodity derivatives* firms is disproportionate?
(p. 64)**

We do not think that the application of the CRD large exposures regime to energy derivatives firms is proportionate. We refer to our answer to question 16. This is even more the case if the MiFID exemptions would not be retained in its current content.

- 26. Do you agree that the maturity ladder approach is unsuitable for calculating capital requirements for non-storable commodities? If yes, are the proposed alternatives better suited to the task?
(p. 67)**

Yes, we agree that the CRD maturity ladder approach seems not suitable for non-storable commodities, as it regularly leads to an overestimation of capital requirements. Current spot prices for electricity and gas do not reflect market expectations for prices on a future delivery dates. As the energy spot prices are very volatile, the

maturity ladder approach tends to overestimate the risks and thus the capital requirements.

The second option discussed in the consultation paper, i.e. an approach that does not depend solely on current forward prices, but instead derives forward prices from a price history over a specified observation period, could be an appropriate approach to mitigate the problem.

27. Do you believe that the shortcomings identified in 2. b. and c. and 3. are relevant? Are there others that need consideration? (p. 69)

We think that the solutions outlined in paras 274-277 to the problems identified in 2c. and 3. are reasonable (2b is not applicable to the energy industry, as it relates to agricultural products).

28. Do you think that the solutions outlined above are adequate to address these problems? (p. 69)

We refer to our answer to question 27.

29. Do you agree with the conclusion above? (p. 71)

As set out in our answers to questions 8 and 10, the differences between the risks connected with energy commodity and the risks connected with other commodity derivative activities/services are considerably lower than the differences between the risks posed by institutions and the risks posed by specialist commodity derivatives firms. Therefore, we think a general commodity regulatory regime is appropriate.

**30. Which of the options presented above do you consider appropriate for the application to *specialist commodity derivative firms*?
(p. 75)**

As set out above, there are strong reasons to retain the content of the current exemptions for specialist commodity derivative firms.

If the content of the current exemptions shall not be retained, we think that Option 1, which is based on qualitative risk management and disclosure framework, could be the basis for an adequate prudential regime for specialist commodity derivative firms. In any case, Option 4 does not seem appropriate for specialist commodity derivative firms and would place disproportionate burdens for the firms concerned.

**31. Do you think a complementary opt-in or opt-out regime could be helpful?
(p. 75)**

If the content of the current exemptions is not retained, a complementary opt-in or opt-out regime could be a reasonable add-on to a specific prudential regime for specialist commodity derivatives firms. At the same time, we like to point out that before implementing such a regime, the criteria and procedures attached with such a regime must be clearly defined (after proper consultation of the market participants).