



## CMCE

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### **Proposed amendments to draft RTS 20 (ancillary activity)**

Dear Tilman,

I am writing to you on behalf of the Commodity Markets Council – Europe (CMCE) and regarding amendments to the draft regulatory technical standard (RTS) 20 for Article 2(4) of Directive 2014/65/EU on markets in financial instruments (MiFID 2). As members of the CMCE we seek practical and proportionate rules for the Article 2(1)(j) MiFID 2 exemption. We consider that draft RTS 20 provides a good basis for these rules. However, we believe that some RTS 20 provisions will lead to consequences unintended by the co-legislators and should be amended by the European Securities and Markets Authority (ESMA). We provide our suggested amendments with justification below.

#### **Capital employed v proxy test**

We do not believe that ESMA's proposed proxy test will ever present an accurate picture of group main business for the purposes of the exemption. We understand why ESMA has proposed this test but we remain sceptical. We do not believe that group-level trading activity is a viable proxy for a group's commercial business and we fear that the proposed test will produce 'false positives' for many commodity producers and consumers, which may deny them use of the exemption.

We consider the test based on capital employed and originally proposed by ESMA to be a better assessment of ancillary activity and the only approach in line with the prescription of Article 2(4) MIFID2. However, as we understand ESMA sees a number of difficulties with a capital employed test, we set out two alternatives below for consideration. We emphasise that of these two alternatives, Alternative 1 is by far our preferred option and we include the second alternative only as fall back.

We note the concerns of ESMA as regards to how capital would be allocated for the purposes of measuring a person's trading activity in commodity derivatives, emission allowances and derivatives thereof. However, we believe that these concerns could be addressed by ESMA either in more prescriptive provisions on allocating capital in an amended RTS 20 or in subsequent guidance for national competent authorities. The proposed delay to application of the MiFID 2 legislation gives ESMA ample opportunity to do so.

#### **Alternative 1: replace capital employed with net turnover**

We consider a test based on net turnover to be a viable alternative to capital employed. Using the definition of "net turnover" in Article 2(5) of Directive 2013/34/EU on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings ("Accounting Directive"), an amended Article 3 RTS 20 would require a person seeking to use the exemption to assess the size of non-privileged trading activity by comparing (a) the net turnover resulting from trading in commodity derivatives, emission allowances and derivatives thereof over a defined accounting period minus net turnover from privileged transactions, and (b) the net turnover of the group over a defined accounting period.

The numerator would include all net turnover arising from non-privileged trading in commodity derivatives, emission allowances and derivatives thereof traded on a trading venue (as defined in MiFID 2) or executed bilaterally by the person seeking the exemption. The denominator would be derived from net turnover of all group activities worldwide.

We propose that ESMA amend Article 3 RTS 20 to introduce a net turnover test. Persons with non-privileged trading activity representing less than 25% of group net turnover would be eligible to use the thresholds in Article 2 RTS 20. Persons with non-privileged trading activity representing more than 25% but less than 50% of group net turnover would be eligible to use 'halved thresholds' (each Article 2(1) threshold x 0.5). Persons with non-privileged trading activity representing more than 50% of group net turnover would be unable to use the exemption as non-privileged trading activity could not reasonably be considered ancillary to that person's main business at group-level.

There are several advantages with this alternative approach. Firstly, it uses a common, uncontested figure defined in Union law. Secondly, it uses data subject to audit requirements and easily verified by national competent authorities. Thirdly, it requires no assumptions as to the main business at group-level.

### **Alternative 2: adopt a revised proxy test**

Again, this is not our preferred option, but should the Commission consider it necessary to maintain ESMA's recommended proxy approach, we propose that Article 3 RTS 20 is amended so as to clarify application and adjust thresholds. Persons with non-privileged trading activity representing less than 25% of group 'main business' using the trading activity proxy would be eligible to use the thresholds in Article 2 RTS 20. Persons with non-privileged trading activity representing more than 25% but less than 50% of group 'main business' using the trading activity proxy would be eligible to use 'halved thresholds' (each Article 2(1) threshold x 0.5). We would suggest that ESMA retain the draft Article 23(2)(b) provision for persons with non-privileged trading activity representing more than 50% of group 'main business'.

However, for the revised proxy test to work at all there must be certainty as to the jurisdictional scope of the test. We propose that Article 3(3) and (4) RTS 20 is amended to clarify that:

- (1) Numerator: gross notional value of person's net non-privileged positions in commodity derivatives, emission allowances and derivatives thereof either (i) traded on a trading venue or (ii) executed bilaterally.
- (2) Denominator: nominal or gross notional value of group's net positions in all financial instruments

By definition (MiFID 2), the numerator would include all EU trading activity of the person seeking to avail of the exemption. The denominator would include all trading activity worldwide by the group to which the person is part.

### **The way forward**

Although our preference is for a capital employed calculation, we consider Alternative 1 to be an acceptable alternative approach to detailing the conditions of the Article 2(1)(j) MiFID 2 exemption and an approach best aligned with the prescription of Article 2(4) of the legislation. Alternative 2 is our least favoured option, but a slight improvement on the ESMA proposal. We believe that the amendments we have proposed in Alternative 1 would ensure that persons whose speculative trading cannot reasonably be considered ancillary to their main business cannot use the exemption without denying the exemption to commodity producers and consumers that use derivative markets principally to manage risks relating to their commercial and treasury financing activity.

Your sincerely,



Jonathan Hill, Chair, Commodity Markets Council Europe