MiFID II in energy trading: The best practices in implementing the ESMA guidelines

MiFID II will have a significant impact on the energy market, and there are a number of unique challenges that will need to be appreciated by market participants if they are to comply with the latest developments that have been made in this area.

Ahead of The application of MiFID II for energy trading Conference, we spoke with Nikos Triantafyllidis, Group Financial and Energy Markets Compliance Manager at OMV, who analyses the best practices in implementing the ESMA draft tests as well as the latest developments in RTS 20.

Could you please determine the relationship between 'speculative' activity and overall market activity within the final ESMA guidelines?

The ESMA guidelines have already introduced the notion of hedging for the purposes of EMIR (Article 10(3) of Regulation (EU) 648/2012) setting the framework for calculating the clearing thresholds applicable to non-financial counterparties relating to contracts objectively measurable as reducing risks directly relating to commercial or treasury financing activity of this counterparty or its group. In this way the remaining market activities fall within the "speculative" area. In light of MiFID II this definition is enhanced in order to form the so called privileged transactions which also include intragroup and liquidity providing market activities as well as elaborations on the required risk management infrastructure aiming in differentiating between hedging and "speculative" activities. The overall market activity encompasses all trading in MiFID II Financial Instruments at EU level either OTC or in trading venues.

Could you explain the threshold levels within the finalized ESMA draft tests?

ESMA sets two separate tests in the latest draft of the Regulatory Technical Standards: a market share and a main business test. The first test sets the allowed thresholds of speculative market activity measured in Gross Notional Value per type of commodity in relation to the overall market size in EU for the relevant asset class as follows: 4% for Metals, 3% for Oil & Oil products, 10% for Coal, 3% for Gas, 6% for Power, 4% for Agricultural Products, 20% for Emission Allowances and finally 15% for all remaining asset classes like Freight. The second test refers to the quantification of the relation between the main and ancillary business activity of a non-financial institution and uses similar calculation logic as the market share test (this is subject to change in order to be approved by the European Commission) by setting the ratio of "speculative" trading activity to the overall market activity of the non-financial institution in direct relation to the market share test as follows: smaller than 10%then the ancillary activity status is accepted, greater than 10% but smaller than 50% then the market share test for the relevant asset class should remain below 50% of the initial value (e.g. for oil this would be 1,5%) and finally for greater than 50% then the market share test for the relevant asset class should remain below 20% of the initial value (e.g. for gas this would be 0,6%).

Could you highlight the latest developments in RTS 20?

The final ESMA draft text on RTS 20 has been recently rejected by the European Commission and certain amendments were requested from EMSA in order the former to endorse it. In particular, the definition of the main business test which according to ESMA is based solely on the Gross Notional Value of the used commodity derivatives is not appropriately reflecting the commercial activity of the non-financial institution since the commercial entities employ various means to hedge their activity, including physical or financial means other than commodity derivatives. Furthermore, in certain instances there exist significant parts of a commercial activity which cannot be hedged or even do not require any hedges. Finally, the proposal of ESMA neglects the often considerable investments in assets conducted by entities and groups that are not reflected in corresponding hedging positions. The optimal solution to this topic would be, as proposed by the European Commission, to re-introduce the capital employed as a possible method of performing the main business test in order to benefit from the ancillary exemption provision in MiFID II.

The MiFID II will have a significant impact in the energy market. Could you please explain how it will impact companies' infrastructure?

The new MiFID legislation package impacts substantially the energy market since it forms the main gate keeper for other pieces of financial regulation like EMIR or MAR. MiFID II directly influences many parts of the energy business as the products offered in the market, the way of doing hedging, or imposes a considerable IT setup which has an immediate effect on budget and cost level. Especially, the energy market liquidity can be reasonably expected to be impacted as small market players enter in a restrained position needing to adjust their limited resources according to the evolving complexity of the financial legislation.

What would you like to achieve by attending the Getting ahead: the application of MiFID II for energy trading conference?

The main aim would be to get up-to-date with the latest developments in the Level 2 MiFID II legislation texts and openly discuss with other market stakeholders the relevant topics concerning the implementation and impact of financial regulations on the existing business models of energy companies within the liberalized European energy market.

About the speaker:

Nikos Triantafyllidis has been with OMV since 2011. He works as Group Financial and Energy Markets Compliance Manager in the corporate compliance department of OMV Group. His principal duty is the group-wide coordination of activities with regard to the implementation of REMIT, EMIR, MiFID II and other related financial regulations. Before joining OMV, Nikos Triantafyllidis spent a number of years working in the Netherlands for various companies in the financial services industry such as International Marketmakers Combination and APX-ENDEX.
He graduated in Physics and holds a MSc degree in Applied Mathematics at the Aristotle University of Thessaloniki in Greece.

About the event:

This **marcus evans** event will give companies the best practices and strategies to comply and align with MiFID II within finalized regulatory guidelines. They will discover and understand scope in terms of speculative hedging, ancillary and physical forwards while proactively restructuring their business model to best align with compliance standards. They will gain an advantage over competitors by hearing from experts that will provide both insight and innovation.

The Getting ahead: The application of MiFID II for energy trading Conference will take place from the 15th until the 17th of June 2016 in UK, London.

For more information about the event, please click here or contact:
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