

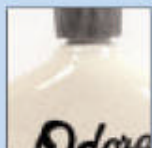
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## MiFID and Commodities Business

Presentation by Claude Unge

Nordic Capital Markets Forum - 12 June 2006



# Overview of items to be covered

Commodities business focus on

- Status under existing regime
- New instruments under MiFID
- Exemptions under MiFID
- Effects of MiFID



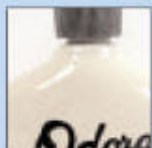
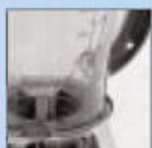
# Status under existing regime

- Commodities business is not subject to
  - Mandatory EU authorisation requirements
  - EU passport regime
  - EU consolidated supervision requirements
- However
  - Member states can impose national authorisation requirements on commodities firms (and many do – regulation different in all Nordic countries)
  - Some unilateral recognition of other member states authorisation



# New instruments under MiFID

- Instruments covered by MiFID listed in Section C of Annex I
- Extension of “financial instruments” definition
  - Derivative contracts relating commodities that (i) must or may be cash-settled; (ii) can be physically settled and traded on a regulated market/MTF; or (iii) can be physically settled other than those under (ii) and not being for commercial purposes having the characteristics of other derivative financial instruments
  - Credit derivatives
  - Contracts for difference
  - Derivative contracts relating to climate variables, freight rates, emission allowances, inflation rates/economical statistics, other assets, rights, obligations, indices, and measures having the characteristics of other derivative financial instruments (i.e. C10 derivatives)
- Definition of “investment firm” is expanded



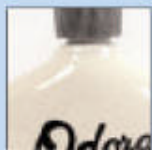
# Exemptions under MiFID

- General issues
  - Where a firm falls within an exemption MIFID does not apply to it
  - Exemptions are listed in articles 2 and 3 of MiFID and apply, *inter alia*, to
    - Insurers
    - Group treasurers
    - Professional investors who invest only for themselves
    - Pension schemes
    - Commodity producers and traders



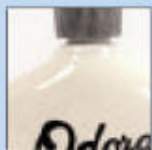
## Exemptions under MiFID (cont.)

- Exemptions relating to commodity business
  - Article 2.1(b) group exemption
  - Article 2.1(d) dealing on own account exemption
  - Article 2.1(i) activity ancillary to main business
  - Article 2.1(k) dealing on own account in commodities and/or commodity derivatives



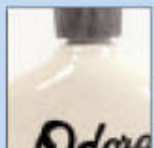
## Exemptions under MiFID (cont.)

- Exemption in article 2.1(b)
  - Potentially relevant to companies providing investment services to other group companies
  - Only applicable to investment services and not activities
  - Investment services must be exclusively for parent undertakings, subsidiaries etc
  - Might be possible for a firm to rely on a combination of articles 2.1(b) and 2.1(i)



## Exemptions under MiFID (cont.)

- Exemption in article 2.1(d)
  - Firm must not provide any investment services or activities except dealing on own account
  - Exemption does not apply to market makers
  - Nor does it apply if you deal on own account
    - Outside a regulated market or an MTF
    - On an organised, frequent and systematic basis by providing a system accessible to third parties in order to engage in dealings with them



## Exemptions under MiFID (cont.)

- Exemption in article 2.1(i)
  - A commodity firm dealing for own account in financial instruments ancillary to the main business of the commodity firm (group basis)
  - A commodity firm providing investment services in commodity derivatives and C10 derivatives can rely on this exemption if the investment service is ancillary to the main business of the commodity firm (group basis)
  - Not clear what “ancillary” means (potentially subject to further European Commission legislation, article 2.3)



## Exemptions under MiFID (cont.)

- Exemption in article 2.1(k)
  - A commodity firm whose main business consists of dealing for own account in commodities and commodity derivatives (provided the group's main business is not investment services/banking)
  - Does not apply to C10 derivatives



## Exemptions under MiFID (cont.)

- Commission to report by 30 October 2007 on
  - Continuation of article 2.1(k) for entities whose main business is dealing in commodity derivatives (not those whose main business is dealing in commodities)
  - Continuation of article 2.1(i) as a whole (not limited to aspects dealing specifically with commodities)



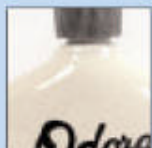
# Effects of MiFID - immediate

- Commodities business passport
  - Banks, mainstream investment firms
  - Specialised commodity trading subsidiaries in banking/investment firm groups (which may fall within exemption in article 2.1(d))
- Outside banking/investment firm groups, no passport
  - Nationally regulated commodity trading firms where e.g.
    - Main business is own account dealing in commodities/derivatives
    - Business is ancillary to group's business within article 2.1(i)
    - Possibly even if an investment firm today (e.g. Sweden)
  - Unregulated commodity producers, manufacturers, generators
    - Providing risk management services taking firm outside article 2.1(d) is likely to be exempt under one of article 2.1(i) or (k)
    - Extent of national regulation depends on national rules (e.g. continuation of "with or through" exemption in the UK)



## Effects of MiFID - possible

- Unlikely to affect entities in banking/investment services groups
- Many nationally regulated (but exempt) commodity firms likely to become investment firms, except where
  - Main business is dealing in physical commodities (article 2.1(k))
  - Some entities whose business is ancillary to group's main business (article 2.1(i))



## Effects of MiFID - likely

- Unregulated commodity producers, manufacturers, generators and their trading affiliates may become investment firms (if deal in derivatives)
- But may be able to
  - Restructure to rely on exemption for entities whose main business dealing in commodities (article 2.1(k))
  - Rely on exemption for business ancillary to group's main business (article 2.1(i))
  - Book business outside the EU, relying on exemptions for cross-border business if booking business with EU counterparts