– Position paper –

Europex post-energy crisis policy recommendations for strengthening the integrity and resilience of commodity derivatives markets

Brussels, 13 June 2024| There is strong and compelling evidence that some of the peaks in the price of European natural gas, which transpired in the summer of 2022, were exacerbated by unconventional buying in day-ahead gas markets, as a direct result of trading activity aimed to fulfil gas storage filling obligations under the EU Gas Storage Regulation. By the end of 2022, to address volatility and elevated price levels in European natural gas, EU emergency measures were agreed, including the Market Correction Mechanism ('MCM'), an Intra-day Volatility Management Mechanism, and review clauses were introduced in the MiFID II commodities derivatives section, which aimed to address perceived inadequacies in the functioning of energy derivatives markets. However, the emergency measures and MiFID review clauses did not consider the principal cause of the price peaks, i.e., the need for certain companies to rapidly find new sources of gas after Gazprom stopped honouring its long-term contracts towards European customers, including entities which were mandated to fill European gas storages ahead of the upcoming winter.

In light of the upcoming review of the MiFID/R commodity derivatives section, Europex recommends that the European Commission adopts a broader perspective, taking into account the impacts of EU emergency legislation on energy derivatives markets.

To this end, we invite the Commission to:

- **Put forward legislative proposals that ensure gas storage filling targets are met in a controlled and diversified manner;**
- **Allow the MCM to lapse, as it poses serious risks to financial stability and security of supply and does not fit with the EU's ambition to foster the CMU, improve its competitiveness and strengthen its strategic autonomy, and;**
- **Refrain from revising the MiFID commodity derivatives section, including the position limits regime, the position management framework and the ancillary activity exemption, as no inadequacies were found in financial markets during the energy crisis following extensive reviews by ACER, ESMA and the ECB.**

1. Ensure Member States meet the gas storage filling targets in a controlled and diversified manner

As increased geopolitical tensions after Russia's invasion of Ukraine amplified uncertainties and highlighted the need for well-filled gas storages for future winters, in June 2022, Member States agreed to install gas storage filling targets according to a strict predefined timeline. Member States were required to fill gas storage sites to at least 80% of capacity by 1 November 2022 and to 90% every 1 November thereafter, until 31 December 2025.

In a report published by ACER and CEER in October 2023[1], it was made clear that, besides the Russian gas supply cuts, costly LNG imports and congested access to LNG terminals and natural gas pipelines, prices were exacerbated by the storage measures the EU adopted in June 2022.

In the summer of 2022, the German market area managers bought large gas quantities at high spot prices without selling these to the forward market. This is in stark contrast with the common practice of simultaneously buying gas in the spot market (in summer) and selling it on the forward market (by using winter maturities). Moreover, there was no transparency on when and how the stored gas would be released to the market. This situation caused great uncertainty among market participants who were expecting downward pressure on the forward price curve.

Europex believes that, if not pursued by professional market participants in a controlled and diversified manner, the trading activity conducted to meet gas storage filling targets has the potential to disrupt national gas markets. To avoid such disturbance, Member States should ensure that regulated entities pursuing filling targets under the Gas Storage Regulation follow a proportionate and diversified trading strategy. This includes using different gas market segments, i.e., spot and derivatives. It appears that until October 2022, the German market area manager did not have access to any futures market. Access to futures markets also ensures that regulated entities have appropriate systems in place to guarantee they are fit and proper to buy and sell large quantities of gas in a controlled manner. This ensures that market participants are aware of best practices for organising the trading function and, furthermore, are not restricted to buying gas on a day-ahead gas market only, rather having the ability to diversify their trading behaviour by trading on financial markets. ACER and ESMA would be best suited to develop principles for market participants pursuing storage filling obligations that prevent uncontrolled buying behaviour. Finally, Member States should provide more transparency on the filling and release trajectories. The VIS study[2] addresses in more detail the situation described above regarding the implementation of national storage measures in Member States and proposes useful recommendations for the future.

[1] ACER-CEER: "European gas market trends and price drivers. 2023 Market Monitoring Report" (October 2023).
[2] ACER/CEER commissioned report by VIS Economic Energy Consultants: "Study on the impact of the measures included in the EU and National Gas Storage Regulations", Volume 2 (February 2024).

To fundamentally improve the robustness and resilience to events like the energy crisis and the trading behaviour that has exacerbated it, Europex strongly recommends amending the Gas Storage Regulation:

- **Requiring market participants to be a member of a regulated market when trading to fulfil gas storage filling obligations under the Gas Storage Regulation;**
- **Mandating ACER, in cooperation with ESMA, to develop principles for market participants pursuing storage filling obligations that prevent uncontrolled buying behaviour, and;**
- **Mandating Member States to provide more transparency on the intermediate filling and release trajectories.**

2. Allow the MCM to lapse

Supervisors, academics, market operators and market participants have all extensively warned about the adverse impact of the MCM, including risks to the EU's financial stability and security of supply. As confirmed in both the preliminary[3] and final[4] reports on the MCM, ACER demonstrates that there has been no observable benefit to the implementation of the MCM Regulation.

These concerns continue to be relevant today. Overall, the MCM poses serious risks to financial stability and security of supply and does not fit with the EU's ambition to foster the Capital Markets Union, improve its competitiveness and strengthen its strategic autonomy[5]. If market participants would ever become concerned about the prospect that the MCM could trigger, the EU's most successful, globally traded energy commodity derivatives market may move outside of the EU. This euro-denominated market would thereby no longer be subject to the EU's regulatory framework and supervision. Moreover, the liquidity in the main hedging tool in Europe, which is designed to smoothen consumer impact to spot gas prices, would be reduced. This would result in consumers being more exposed to gas price volatility, increasing the cost of capital of the European energy industry and reducing their competitiveness.

To improve the EU's competitiveness and strengthen its strategic autonomy, Europex strongly recommends discontinuing the MCM at the earliest opportunity.

3. Refrain from revising the MiFID/R commodity derivatives section

In early 2024, the European Parliament and Council adopted amendments to the Markets in Financial Instruments Regulation (MiFIR) and Markets in Financial Instruments Directive (MiFID II). Regarding commodity derivatives trading, Article 90(5) of the amended MiFID II gives a mandate to the European Commission to assess the ancillary activity exemption, the position limits regime and the position

[3] ACER: "Market Correction Mechanism: preliminary data report" (23 January 2023).
[4] ACER: "Market Correction Mechanism, effects assessment report" (1 March 2023).
[5] The European energy crisis, the Dutch TTF and the other market correction mechanism: a financial markets perspective", Ebbe Rogge, Journal of World Energy Law and Business (2024).

management framework, as well as the potential streamlining of transaction reporting streams and decide on potential changes. The mandate was decided upon in the wake of the energy crisis and followed a political sentiment that energy derivatives markets were subject to inadequacies. From our perspective, however, energy derivatives markets have proven highly resilient and performed exactly as expected, providing essential transparency on the supply scarcity and allowing market participants to hedge their price and volume risk right when it was most needed. Different reviews by ACER[6], ESMA[7] and the ECB[8] confirm this view. ESMA considers that despite the record natural gas prices, there has been no extreme volatility or illiquidity, to conclude that natural gas markets continued to function appropriately during the August 2022 market events. The ECB confirms that speculation played a limited role above and beyond hedging needs and, despite many accusations in the political arena, it did not amplify the transmission of fundamental shocks.

Moreover, in 2021, in response to the COVID-19 pandemic, a number of amendments to MiFID II (i.e., the "Quick Fix") were introduced in relation to commodity derivatives, including the ancillary activity exemption, the position limits regime and position management framework. Specifically, the reduction in scope of the position limits regime have removed a key obstacle for the growth of nascent and less liquid contracts that have allowed market participants to be better hedged during the crisis. As explained in a recent study from Luther and Frontier Economics that addresses principles of energy market regulation[9], the current ancillary activity exemption is properly calibrated, ensures proper market functioning and efficient risk management by market participants. If the current framework of the ancillary activity exemption was to be substantially modified, the liquidity of both physical and financial energy markets as well the competitive position of EU market participants in globally traded markets would be negatively impacted.

In absence of any clear rationale for additional reforms and to provide a stable and predictable regulatory environment in line with the better regulation principles, Europex strongly advises to refrain from introducing further substantial reforms in the MiFID commodity derivatives section.

[6] ACER-CEER: "European gas market trends and price drivers. 2023 Market Monitoring Report" (October 2023).
[7] ESMA: TRV Risk Analysis, "The August 2022 surge in the price of natural gas futures" (24 October 2023).
[8] ECB: "Speculation in oil and gas prices in times of geopolitical risks", report published as part of the ECB Economic Bulletin, Issue 2 (2024).
[9] Frontier Economics/Luther: "Principles of energy market regulation – securing efficient & resilient energy trading", prepared for Energy Traders Europe (19 April 2024).

About

Europex is a not-for-profit association of European energy exchanges with 33 members. It represents the interests of exchange-based wholesale electricity, gas and environmental markets, focuses on developments of the European regulatory framework for wholesale energy trading and provides a discussion platform at European level.

Contact

Europex – Association of European Energy Exchanges
Address: Rue Archimède 44, 1000 Brussels, Belgium
Phone: +32 2 512 34 10
Website: www.europex.org
Email: secretariat@europex.org
Twitter: @Europex_energy

EU Transparency Register: 50679663522-75