FIA EPTA response to FCA CP23/27 on reforming the commodity derivatives regulatory framework

16 February 2024

FIA EPTA welcomes the opportunity to respond to the FCA's proposals for reforming the UK commodity derivatives regulatory framework. We have consistently supported the objectives of the Wholesale Markets Review and wider Edinburgh Reforms to ensure a proportionate and effective regulatory regime for the UK wholesale markets, on which FIA EPTA's members, acting as principal trading firms, are important providers of liquidity to end-investors. This includes the UK commodity derivative markets, where we observe increasing participation by principal trading firms, helping to diversify liquidity flows to the benefit of other participants on these markets and contributing to the overall attractiveness and competitiveness of the UK wholesale markets more generally.

FIA EPTA's members support the FCA's objectives of promoting market integrity and resilience and preventing disorderly trading and settlement in the commodity markets and our members generally welcome the proposals included in the consultation. We restrict our comments, therefore, to a limited number of issues, as set out in our response below.

We appreciate your consideration of our comments and remain available to discuss any of these issues further with the FCA.

Implementation timelines

FIA EPTA members note the FCA proposes a transitional period of one year to enable market participants to make the necessary changes to comply with the new regime. We would caution that this proposed transitional period does not demarcate the time for (i) trading venues to make relevant rule changes; (ii) the FCA to review these proposals and provide feedback on these changes, and finally (iii) for other market participants to take practical steps to implement any new requirements following from these changes.

In this regard, FIA EPTA members expect that a period of only one year will not be sufficient to complete these three steps, given the likely significant workload related to the regulatory change process by the venues and the subsequent implementation thereof. The more so, as trading venue rule amendments typically require extensive industry dialogue and consultation and following this, market participants will still require sufficient time to implement any operational changes they need to make.

We would suggest, therefore, a period of 18 months for trading venues to complete rulebook changes with a further period for implementation which should have regard to the complexity of venue proposals. The specific subsequent timeframe for market participants to implement the required changes should be determined as part of the exchange member consultation process.

Setting of position limits

Regarding Chapter 4 of the Consultation Paper, FIA EPTA members are supportive of the approach for the FCA to identify critical contracts in scope of the commodity derivatives regulatory framework, and the FCA's proposed methodology for doing so. We are also supportive of the approach for trading venues to set the position limits given their proximity to the contracts. We further agree that the current fixed position limit thresholds are not suitably flexible or proportionate for certain contracts, and agree with the proposed factors that trading venues will have to take into account for their setting of position limits.

However, we do have concerns regarding the potential divergences of position limits practices across different trading venues, given the proposed flexibility over the setting of such position limits. It is obviously understood that the FCA will be supervising the trading venue's methodology of the setting of position limits, however we would urge for the FCA to ensure pro-active and holistic supervision over this area. We would emphasise that undue divergence between position limits across trading venues would cause operational and reporting burdens for firms trading the same critical commodity contracts across different trading venues. This could also create divergences that would lead to firms preferring to trade critical contracts on trading venues with more relaxed position limits.

Similarly, we agree with allowing trading venues to identify related contracts for each critical contract for the purposes of commodity derivatives position limit reporting. However, the criteria set out in Chapter 3 of the Consultation Paper will likely encompass a significant number of contracts. This could increase operational burdens for reporting firms, and depending on trading venue's interpretations this could lead to discrepancies between the venues. Therefore, again, we would reiterate the need for the FCA to ensure pro-active and holistic supervision when determining a trading venue's methodology.

New reporting requirements

FIA EPTA members appreciate the importance of monitoring the proper functioning of the commodity derivatives markets. However, we would strongly question the need for any additional reporting obligations for firms trading on UK derivatives markets. FIA EPTA's members and other firms already report positions to trading venues under the MiFID II Commodity Position Reporting regime. From a cost-benefit perspective, we would encourage the use of the existing Commodity Position Reporting regime for any additional data that trading venues need to collect in order to adequately set and monitor usage of position limits on their venues, and to not create any additional reporting framework for this purpose.

Liquidity provider exemptions

FIA EPTA members are highly supportive of the FCA's proposed liquidity provider exemption. However, we note that some exchanges can enter into 'best efforts' liquidity provider schemes with their members. As these 'best efforts' schemes support liquidity provision and efficient price formation we would welcome for the FCA to consider broadening the liquidity provider exemption to include all contractual exchange liquidity schemes. Such expansion of the liquidity provider exemption to encompass 'best efforts' liquidity provider schemes would be easily administered by

exchanges who negotiate contractual terms with their members. 'Best efforts' liquidity provider schemes encourage exchange members to maintain and grow liquidity on regulated markets, ensuring transparent price formation, deeper liquidity and more robust and competitive markets. For these reasons, we consider that the additional application of the liquidity provider exemption to such 'best efforts' schemes would further help to strengthen the efficiency and over-all functioning of the UK commodity derivative markets.

About FIA EPTA: The European Principal Traders Association (FIA EPTA) represents the leading Principal Trading Firms in the EU and UK. Our members are independent market makers and providers of liquidity and risk transfer for markets and end-investors across Europe, providing liquidity in all centrally cleared asset classes including shares, bonds, derivatives and ETFs. FIA EPTA works constructively with policymakers, regulators and other market stakeholders to ensure efficient, resilient and trusted financial markets in Europe. More information about FIA EPTA and independent market makers is available on: www.fia.org/epta and www.wearemarketmakers.com