Montel: New rules could double energy market spreads – Efet

(Montel) The European Federation of Energy Traders (Efet) is “seriously concerned” legislation unveiled this week could drive up trading costs by doubling bid-offer spreads on energy markets, board chairman Paul Dawson told Montel.

The European markets authority Esma published on Monday its final draft of “regulatory technical standards” (RTS) that flesh out the incoming Mifid II financial market directive.

“The top level concern is what is described as the ‘main business test’,” said Dawson, who is also head of regulatory affairs at Germany’s RWE Supply and Trading.

It is “not unreasonable” to assume that the measure could lead to a doubling of bid-offer spreads on European energy markets, adding EUR 3bn to consumers’ power, gas, coal and oil costs, Dawson said.

Efet has long argued that bringing energy traders under financial market regulation would reduce liquidity as small and medium-sized players exit the market rather than take on onerous Mifid licensing costs and capital requirements.

Exemption test
In terms of the main business test, Dawson was referring to part of a two-pronged Mifid II exemption test where firms must prove that their speculative derivatives trading is subsidiary to their main business activity, such as power generation or retail.

Esma has decided that this should be established by measuring a firm’s non-hedging trades as a proportion of their overall commodity derivatives trading, with the threshold set at 10%.

However, Efet said total derivatives trading is not an accurate reflection of the size of a firm’s main business.

“It completely ignores the fact that you might have lots of other assets like a distribution grid, or a completely unrelated main business or asset that isn’t being hedged through commodity derivatives,” Dawson said.

Uncertain impact
The Efet chairman was unable to detail which firms face being drawn into full financial regulation if Esma’s proposed test remains in its present form.

“The feedback from members is that those concerns cut pretty deep and it’s not just the larger usual suspects,” Dawson said in reference to Europe’s major utilities firms.

The lobby group said the main business test is not in line with the Mifid II directive adopted by EU lawmakers last year and due to take effect in January 2017.

“I think there are sufficient grounds to have another look at this,” Dawson said.

This view was shared by Conor Foley of law firm Norton Rose Fulbright, who sees Esma’s main business test as “problematic” from a legal point of view.

Those seeking to use exemption will have many activities and investments, such as energy infrastructure, which they do not seek to hedge with commodity derivatives or emissions allowances, Foley said.

“If the exemption does not include such activities and investments in the calculation then it does not comply with Mifid II,” he said.

The European Commission has three months to endorse the legislation drafted by Esma. The European Parliament and EU member states would then have a scrutiny period of up to six months before voting the Mifid II small print into law.

Mifid II is a reform of the EU's core financial market regulations in response to the 2008 financial crisis, intended to make Europe's financial markets more resilient and transparent.

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