Finance Watch

Making finance serve society

Finance Watch comments on the Consultation Paper on MiFID II/MiFIR Technical Standards

Brussels, 2 March 2015

Finance Watch is an independent, non-profit public interest association dedicated to making finance work for society. It was created in June 2011 to be a citizen's counterweight to the lobbying of the financial industry and conducts technical and policy advocacy in favour of financial regulations that will make finance serve society.

Its 70+ civil society members from around Europe include consumer groups, trade unions, housing associations, financial experts, foundations, think tanks, environmental and other NGOs. To see a full list of members, please visit www.finance-watch.org.

Finance Watch was founded on the following principles: finance is essential for society and should serve the economy, it should not be conducted to the detriment of society, capital should be brought to productive use, the transfer of risk to society is unacceptable, and markets should be fair and transparent.

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Only the questions that are relevant to Finance Watch are reproduced here.

We agree with the publication of this response.

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3. Transparency

3.10. Double volume cap mechanism and the provision of information for the purposes of transparency and other calculations (RTS 10)

Q86. Do you agree with the articles on the double volume cap mechanism in the proposed draft RTS 10? Please provide reasons to support your answer.

Yes, we fully support ESMA's approach when it comes to implementing the double volume cap mechanism prescribed at Level 1.

While we acknowledge the technical challenge around collecting and aggregating robust and exhaustive data, there is no doubt that the added value of such increased transparency outweighs the burden.

4. Microstructural issues

4.3. Market making, market making agreements and marking making schemes (RTS 15)

Q104. Do you agree with the proposed draft RTS? Please provide reasons for your answer.

Our view is that indeed the RTS constitutes a helpful step forward following the drafting of the discussion paper.

This being said, our main concern is that today so-called liquidity providers only provide liquidity where it is abundant already, while there is little incentive for firms to make markets in lesser liquid instruments (e.g. SMEs). It would therefore make sense to specify that access to incentives should be inversely proportional to the liquidity of the instrument. On a similar note, providing liquidity in stressed market conditions should not have to be specifically incentivized, as it is at the core what is expected from a liquidity provider. On the contrary, so-called market makers that exit the market any time it is not in their favour should see their incentives go down across-the-board, i.e. including in normal times.

4.4. Ratio of unexecuted orders to transactions (RTS 16)

Q109. Do you agree with the proposed regulatory technical standards? Please provide reasons for your answer.

It is very disappointing that ESMA had to step back from its initial ambition of proposing *"…that a maximum should be set out by observing the average OTR on a given electronic trading venue per group of financial instruments and by capping it using a multiplier "x" to be set and reviewed at least on an annual basis*", after the Commission *"…specified that this proposal would not fall within the scope of the draft regulatory technical standards (RTS) to be developed under Article 48(12) of MiFID II*" (Consultation Paper, pages 395-396, point 3).

In our view, the record of Level 1 negotiations (four-column table, row 935) shows the intent of the co-legislators for the RTS to set out the maximum ratio of unexecuted orders to transactions that may be adopted by regulated markets.

We doubt that the RTS as currently drafted will contribute to lowering the impact of algorithmic trading systems on disorderly trading conditions on the market.

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4.5. Co-location and fee structures (RTS 17)

Q117. Do you agree with the proposed draft RTS with respect to fee structures? Please provide reasons for your answer.

While "*some attention was drawn to the practice of the maker-taker model and the payment-for-order-flow since they may have negative effects on the markets*" but ESMA considers there is "*insufficient evidence*" of such negative effects at this stage, it would be helpful if ESMA would commit to re-visiting the RTS as further evidence comes forward.

4.6. Tick sizes (RTS 18)

Q123. Do you agree that the average number of trades per day should be considered on the most relevant market in terms of liquidity? Or should it be considered on another market such as the primary listing market (the trading venue where the financial instrument was originally listed)? Please provide reasons for your answer.

Yes, we agree that the most relevant market in terms of liquidity should be the reference, given the recent market structure evolution.

More generally, we are supportive of the "compromise" proposed by ESMA on tick sizes. Any further lowering of its ambition (i.e. allowing for even smaller tick sizes than currently proposed) would make it highly improbable that the regime would lower the occurrences of disorderly market conditions – let alone the potential for gaming.

7. Commodity derivatives

7.1. Ancillary Activity (RTS 28)

Q168. Do you agree with the approach suggested by ESMA in relation to the overall application of the thresholds? If you do not agree please provide reasons.

We agree with the methodology.

Q169. Do you agree with ESMA's approach to include non-EU activities with regard to the scope of the main business?

No, we disagree on the denominator for the ancillary activity test as defined in RTS 28 Article 3.2, which like the numerator should be based on EU and not global capital employed. We therefore recommend to delete the words "*and in third countries*" from this article.

To limit the numerator of the ancillary activity calculation to EU activities, and yet include all activities in third countries in the denominator is deeply inconsistent. European derivative markets are about 29% of all OTC derivatives (http://www.bis.org/statistics/dt1920a.pdf) and 33% of all listed derivatives (http://www.bis.org/statistics/r_qa1412_hanx23a.pdf). Therefore, to exclude two thirds of derivatives activities from the numerator while including all commercial activities in the denominator dilutes the test massively.

Two possible approaches are more logical. The first is to require any firm operating in European derivatives markets to run the calculation using their global derivatives activities in the numerator and their global commercial activities in the denominator. The second is to restrict both numerator and denominator to EU activities.

With the global numerator and denominator approach, there is a concern that a firm with concentrated EU derivatives operations yet distributed global commercial activities could fall out of scope of MiFID. Considered globally, such a firm may have less than 5% of all activities be derivatives-related, yet within Europe perhaps 25-50%. For such a firm to fall outside of MiFID is clearly contrary to the Level 1 legislative intent to bring non-financial firms active on EU commodity markets into scope of MiFID, in line with the G20 Pittsburgh commitments. Of course, the likelihood of such a "false negative" is even further increased by considering EU activities in the numerator but global activities in the denominator, as in the current proposal.

Therefore, the EU numerator and global denominator test should be rejected and replaced by the far more accurate EU-based numerator and denominator test.

Q171. With regard to trading activity undertaken by a MiFID licensed subsidiary of the group, do you agree that this activity should be deducted from the ancillary activity (i.e. the numerator)?

No, as this would transform the ancillary activity threshold into an allowance.

As ESMA recognizes in its analysis, Recital 20 shows the intent of the co-legislators to cover non-financial firms whose activity on financial markets is disproportionate to their main business. In our view, this drafting suggests that the trading activity test should be defined as a threshold, above which a firm must become MiFID-compliant for all its activities, and not as a de facto "[speculative] allowance" of 5% of activities which can always be performed outside of MiFID (subject to putting the required organisational structure in place).

The co-legislators agreed to widen the scope of MiFID beyond the MiFID I exemption for dealing on own account, and to explicitly cover non-financial firms acting on financial markets, while at the same time giving exemptions of individual MiFID obligations. In line with this logic, the ancillary activity test was introduced.

A market operator could structure its business to maximize the amount of non-privileged transactions outside of the MiFID-licenced subsidiary, close to the ancillary activity threshold.

Given ESMA's proposed threshold of 5%, a firm could make sure that (slightly less than) 5% of its market activity is outside of the subsidiary, and accept that its privileged transactions plus the non-privileged market activity above 5% are subject to the rules applied to the MiFID-licensed subsidiary. The 5% then becomes an "allowance" outside of MiFID rather than a threshold.

Q172. ESMA suggests that in relation to the ancillary activity (numerator) the calculation should be done on the basis of the group rather than on the basis of the person. What are the advantages or disadvantages in relation to this approach? Do you think that it would be preferable to do the calculation on the basis of the person? Please provide reasons. (Please note that altering the suggested approach may also have an impact on the threshold suggested further below).

We agree with ESMA that the calculation of the numerator should be done at group level, and not on the basis of the person.

In line with our comment on Q171, applying the ancillary activity test on a person basis rather than a group level, would create arbitrage possibilities and allow non-financial firms to set up legal entities solely for the purpose of avoiding MiFID-compliance.

Even more importantly, Recital 20 prescribes the ancillary activity test to be assessed at group level, leaving no possibility for a different interpretation: "*…provided that that activity is an ancillary activity to their main business on a group basis*".

Q173. Do you consider that a threshold of 5% in relation to the first test is appropriate? Please provide reasons and alternative proposals if you do not agree.

Yes, we agree. 5% is a typical margin level on exchange-traded derivatives (and, increasingly, on OTC derivatives). That equates to 20x leverage. Therefore, 5% of activities represents the maximum point at which the entire balance sheet is not yet leveraged by the derivatives portfolio. Any higher, and the entity is wagering more capital than they own, which clearly cannot be considered a "minority of activities".

In fact, with netting arrangements many derivatives books will be more than 20x leveraged.

Moreover, even mildly exotic derivatives can generate highly convex exposures (in fact, it is possible to create massive convexity with even plain vanilla options). The exposure of such derivatives increases exponentially (and in some cases more than exponentially) in adverse market conditions. If a portfolio contains exposures of this sort, statically calculated leverage (e.g. 20x) may dramatically understate the true risks of the derivatives book.

The significant reduction of the threshold to meet G20 requirements is sensible and 5% should be considered a fair upper limit. If a firm has a derivatives book that is 20 times leveraged, which is not uncommon, a 5% allocation of capital to non-hedged derivatives trading would create liabilities equivalent to the firm's entire capital base, and this would be a significant systemic risk for the market.

Q174. Do you agree with ESMA's intention to use an accounting capital measure?

While we continue to prefer risk-weighted capital, we can accept the balance found in the current proposal between the numerator and the denominator.

Q176. Do you agree with the proposal to use the gross notional value of contracts? Please provide reasons if you do not agree.

Yes, we agree. One of the stated purposes of MiFID II is to reduce systemic risk. Allowing netting would potentially exclude from the scope of MiFID (through the ancillary activity exemption) market participants who could have a systemic impact on financial markets.

Q177. Do you agree that the calculation in relation to the size of the trading activity (numerator) should be done on the basis of the group rather than on the basis of the person? (Please note that that altering the suggested approach may also have an impact on the threshold suggested further below)

Yes, see Q172. Recital 20 in our view cannot be interpreted otherwise.

Q179. Do you agree with the threshold of 0.5% proposed by ESMA for all asset classes? If you do not agree please provide reasons and alternative proposals.

As outlined in our response to the Discussion Paper, we prefer ESMA to set a threshold of 0.25%. We do agree that the same threshold should be set for all asset classes.

The Level 1 text clearly specifies that the second test should measure the size of an entity's "*trading activity compared to the overall market trading activity in that asset class.*" Therefore, the test must be performed on a per-asset class basis.

It is true that markets in different asset classes may have different inherent degrees of concentration such that the same percentage of market share in one may confer more market power than in another. In some cases, a percentage of market share below 0.25% could confer sufficient market power as to render the trading activities in question non-ancillary.

However, such cases will be marginal, and in no event is a share of 0.25% insignificant (typically, on US exchanges, existing reporting thresholds are an order of magnitude smaller - http://www.cmegroup.com/market-regulation/position-limits/). Therefore, it is appropriate to set the threshold test at a maximum of 0.25% across all asset classes.

Q180. Do you think that the introduction of a de minimis threshold on the basis of a limited scope as described above is useful?

No. We do not think the Level 1 text leaves any scope for the introduction of a *de minimis* threshold, and certainly not on the ancillary activity test.

The purpose of the double test is to create a reasonable exemption for non-financial firms with a very limited activity on commodity markets (the ancillary activity test), subject to a backstop protecting markets (the trading activity test), and not the other way around. Therefore, the ancillary activity test should always be applied upon mandatory notification to the competent authority.

Recital 20 requires that "*Those criteria should ensure that non-financial firms dealing in financial instruments in a disproportionate manner compared with the level of investment in* *the main business are covered by the scope of this Directive*", and the only way to do so is by applying the ancillary activity test (and applying it first).

Q182. Do you agree with ESMA's conclusions in relation to the period for the calculation of the thresholds? Do you agree with the calculation approach in the initial period suggested by ESMA? If you do not agree, please provide reasons and alternative proposals.

No, we do not agree. While we agree with the need for transition measures, we cannot accept the three year rolling average as a general principle.

A three year rolling average would allow a firm to avoid regulation for up to three years after becoming a sizeable trader. If a hedge fund after two years of business would decide to move into commodities trading, it may be a large player straight away yet exempt for one or two years due to the initial two years of no activity in commodities markets.

7.2. Methodology for calculating position limits (RTS 29)

Q183. Do you have any comments on the proposed framework of the methodology for calculating position limits?

We support the framework methodology although we disagree on the calibration of the baseline position limit. See answer to Q184 for further detail.

Q184. Would a baseline of 25% of deliverable supply be suitable for all commodity derivatives to meet position limit objectives? For which commodity derivatives would 25% not be suitable and why? What baseline would be suitable and why?

The baseline limit is far too high. We think that a general limit of 10% with limited flexibility (e.g. +/- 5%) is more appropriate. We demonstrate below why we believe ESMA's suggested drafting is not in line with the legislative intent.

We should assume that in most cases the national supervisors will choose the upper boundary for the flexibility, i.e. in practise most limits will be set at 25 + 15 % unless there are manifestly abusive positions. If limits were to be set at 25+15% or at 25+10%, three market participants could collectively control the entire market, without breaking the position limits.

Setting the limit at 25+15% would, in our view, not satisfy the Level 1 requirement that position limits should aim to "*prevent[ing] market distorting positions*".

While only the Level 1 text as published in the Official Journal is binding, we believe it is useful to recall some of the political reasoning behind the final drafting of Article 57, in order to secure acceptance of ESMA's Draft Technical Standards by the co-legislators.

The text "*preventing market distorting positions*" was inserted in the Level 1 text at the final trialogue on 14 January 2014 on the explicit request of the European Parliament negotiating team as a condition for final agreement on the Level 1 text. The text replaced a much weaker drafting suggestion by the Greek Presidency which read "*prevention of cornering the market*". This is text is therefore extremely significant from a political perspective.

"*Cornering the market*" is generally understood to refer to market abuse behaviour. (see for example Dodd-Frank Section 737(a)(3)(B)(ii): "*to deter and prevent market manipulation, squeezes, and corners"*)

Having made the change to Article 57 as explained above, we understand that it was the co-legislators' explicit intent to require position limits to not only prevent (individual) cases of market abuse (cornering the market), but also prevent the build-up and existence[1] of positions that (simply) distort the market. To do so, the base position limit arguably must be set much lower than the suggested 25%.

[1]Unlike in the United States under the relevant CFTC Rule, the EU position limits regime requires a continuous assessment of positions, as per Level 1 requirements to set "*limits on the size of a net position which a person can hold*" (Article 57.1)

Q185. Would a maximum of 40% position limit be suitable for all commodity derivatives to meet position limit objectives. For which commodity derivatives would 40% not be suitable and why? What maximum position limit would be suitable and why?

A market with a 40% limit is one in which one single trader can hold contracts conferring ownership of almost half the available supply of a commodity, even in the days approaching contract expiration. This is a ready-made scenario for market manipulation, excessive volatility, and lack of convergence between contract prices and underlying prices.

With a 40% limit, a concert agreement between just three large traders each holding the maximum allowed position and exercising the physical settlement option would result in claims on an exchange exceeding the entire available supply of a commodity, a catastrophic outcome.

Finally, a market in which one trader can hold contracts worth 40% of deliverable supply encourages situations in which excessively large liquidations can occur. Such liquidations often have a knock-on effect, so such a high limit would increase contagion and systemic risk. A trader holding 40% who must suddenly liquidate that position (perhaps because of losses in another market) will almost certainly cause a sudden large drop in prices. This is likely to trigger stop-losses for other traders who must, in their turn, liquidate their positions, creating a domino effect.

This risk persists at lower levels, but is considerably less likely than at the 40% level. Therefore, particularly in the spot month there should never be the capacity for competent authorities to set a limit higher than 10+5% of deliverable supply.

Q188. Do you consider the methodology for setting the spot month position limit should differ in any way from the methodology for setting the other months' position limit? If so, in what way?

The spot month is particularly vulnerable due to the proximity of the contract to expiration. For this reason, exchanges apply tighter limits in the spot month. In line with this market practise, ESMA should ensure that spot month limits are capped at the baseline level, with no significant leeway for competent authorities to raise them.

The specific vulnerabilities of the spot month include:

- Greater susceptibility to manipulation;
- More volatility when large positions are put on or liquidated;
- The possibility for derivatives prices to become decoupled from the price of the underlying commodity, damaging the effectiveness of hedges.

For all these reasons, the spot month limit must be held stable at a low level of deliverable supply. We propose to instruct national authorities to set this limit as close to the baseline level as possible.

Q189. How do you suggest establishing a methodology that balances providing greater flexibility for new and illiquid contracts whilst still providing a level of constraint in a clear and quantifiable way? What limit would you consider as appropriate per product class? Could the assessment of whether a contract is illiquid, triggering a potential wider limit, be based on the technical standard ESMA is proposing for non-equity transparency?

We do not agree that the development of new commodity derivative contracts must lead to higher position limits (RTS 29 Article 8.1). Since the position limits are tied to deliverable supply, and not open interest, there is no need to widen limits for new and illiquid contracts. Allowing one trader to amass an enormous position as compared with the physical stock of a commodity is neither a necessary nor worthwhile step to promote trading in a new contract.

Indeed, any contract which cannot find sufficient interest to generate liquidity within a structure where each individual is permitted to trade up to 10% or even 25% of deliverable supply is clearly failing for reasons other than the position limit. For example, the contract specifications may not be useful to market participants.

Moreover, setting a wider limit for new or illiquid contracts might actually have the opposite effect from that desired. Why would a small trader enter a marketplace in which they know the largest traders can control up to 40% of the deliverable supply? Such a contract would be prone to manipulation and excessive volatility, so the wider limit would deter new participants. Thus, a wider limit could in fact damage liquidity.

Q195. For what time period can a contract be considered as "new" and therefore benefit from higher position limits?

Although we do not support increased position limits for "new" contracts (see answer to Q189), at the very least any "grace period" should be based on the actual characteristics of the market in that contract.

For instance, if a contract is immediately traded heavily, it should be subject to position limits which are not higher than in other markets so as to avoid circumventing of position limits and distorting market positions. In any event, there is no need for such a period to last longer than a year.

Q197. Do you have any further comments regarding the above proposals on how the factors will be taken into account for the position limit calculation methodology?

Regarding volatility, we support the draft text in RTS 29 Article 5. This article reflects the Level 1 text which requires that increased volatility leads to lower position limits. However, we strongly object to ESMA's single-sided assessment of the relationship between position limits and volatility in the consultation paper.

ESMA notes in paragraph 11 of the Background section that "*several respondents*" have argued that volatility "*typically*" arises from a lack of liquidity and that therefore position limits should be set rather generously, to avoid dampening liquidity. This is reflected in paragraph 29 of the consultation paper, where ESMA (only) proposes that "*the competent authority makes any adjustment in line with the following principle: i. position limits should not further increase volatility, by, for example, being so restrictive they drive liquidity from the market*", without requiring national authorities to take into account the positive impact that position limits have on reducing volatility.

The underlying false assumption is that higher levels of trading by non-hedgers necessarily increase liquidity and reduce volatility. On the contrary, in a regime of (relatively generous) high position limits, price volatility attracts momentum trading, which further exacerbates the volatility. Indeed, this is precisely the sort of trading unrelated to supply and demand that position limits aim to curb, in line with the Level 1 drafting that requires position limits to "*prevent[ing] market distorting positions*".

Numerous academic studies support this view. For example, Shen et al[2] (2004) have shown that non-commercial traders are, on the whole, momentum traders; Tang and Xiong (2012) have found that large inflows from non-commercial participants help explain the large spike in commodity price volatility around 2008; and Buyuksahin and Robe (2012) have demonstrated that increased participation in commodity markets from non-hedging traders can cause commodity prices to cross-link with other markets, thus distorting them from their pure supply-and-demand levels.

The legislative intent that increased volatility should further strengthen, not weaken, position limits to protect end-users is clearly reflected in Recital 125: "*The G20 summit in Pittsburgh…agreed to improve the regulation…of financial and commodity markets to address excessive commodity price volatility… the G20 summit in Cannes… called for market regulators to have formal position management powers, including the power to set ex ante position limits as appropriate*".

Therefore, ESMA's drafting proposed in RTS 29 Article 5 is in line with the Level 1 intent and should be maintained as-is (without further weakening carried over from the consultation paper).

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Shen et al: http://citeseerx.ist.psu.edu/viewdoc/summary?doi=10.1.1.197.2419
Tang & Xiong: http://www.princeton.edu/~wxiong/papers/commodity.pdf
Buyuksahin & Robe: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1707103

Q198. Do you agree with ESMA's proposal to not include asset-class specific elements in the methodology?

Yes. While markets differ, the position limits regime as proposed, using relative percentage-based limits and taking into account market structure, is flexible enough to be applied to all asset classes.

7.3. Application of position limits (RTS 30)

Q200. Do you agree with the proposed draft RTS regarding risk reducing positions?

No, we do not agree that the treatment of risk reduction positions must be *identical* to EMIR.

Recital 21 of the Level 1 text requires ESMA to treat risk reducing positions in a way that is "*consistent*" with the treatment in EMIR. However, this does not mean the treatment must be identical. And indeed, a consistent approach requires considering the differences in the two Directives as well as their similarities. Crucially, MiFID II provides a blanket exemption based on two threshold calculations, each of which depends heavily on the definition of “objectively risk reducing positions”. In contrast, EMIR contains no such exemption.

For this reason, it is entirely appropriate and consistent to apply a stricter definition of objectively risk reducing positions for the purpose of the MiFID II technical standards.

Specifically, clause (a) should be modified to remove anticipatory hedging from the definition of “objectively risk reducing”, since such positions can only be properly appraised after the fact, and even then are clearly anything but “objectively measurable” due to their probabilistic nature.

Additionally, clause (b) of the currently proposed definition should not apply in the present case. This clause includes as “objectively risk reducing” any position which covers risks arising from “*the potential indirect impact on the value of assets, services, inputs, products, commodities or liabilities … resulting from fluctuation of interest rates, inflation rates or foreign exchange rates*”. The “potential indirect impact” of an interest rate change on “*assets … or liabilities that the non-financial counterparty … reasonably anticipates owning*” is an extremely liberal interpretation of “*positions objectively measurable as reducing risks directly related to the commercial activity*” of a non-commercial entity. Such a permissive definition is inappropriate to the MiFID II context, in which the risk-reducing definition is of such central importance.

Q203. Do you agree with ESMA’s proposal that a person’s position in a commodity derivative should be aggregated on a ‘whole’ position basis with those that are under the beneficial ownership of the position holder? If not, please provide reasons.

Yes. Double counting should not be an overriding concern. The alternative would lead to under-reporting and given the purpose of position limits, it would be more damaging to have “false negatives” than “false positives”.

It is clear from the Level 1 text that broad inclusion in the new regime is an overarching goal, in line with the G20 commitment to reduce systemic risk and promote regulation of the vast majority of listed and OTC derivatives. Investment firms are explicitly included and very few types of entity with involvement in commodities markets are explicitly excluded. Furthermore, the Level 1 text explicitly mandates consideration of entities at the group level to avoid creating loopholes.

The only potential objection to considering ‘whole’ positions is that in marginal cases it may lead to double counting of positions. However, such a scenario will only arise in those rare cases where control of a subsidiary is in doubt. Due to the already ambiguous nature of such an arrangement, it is far better to err on the side of over-reporting than under-reporting.

Otherwise, firms will have a strong incentive to circumvent the rules by proliferating subsidiaries with ambiguous explicit control agreements.

Q204. Do you agree with the proposed draft RTS regarding the criteria for determining whether a contract is an economically equivalent OTC contract?

Yes. Although we agree with the definition of economically equivalent in the proposed RTS 30 we repeat our earlier concern that optionality should not enable a contract to fall out of economic equivalence.

Q205. Do you agree with the proposed draft RTS regarding the definition of same derivative contract?

No, we think the definition can be further improved.

When the same commodity derivative is traded on competing venues, it will be subjected to the same position limit, and the limit will be set by the competent authority with jurisdiction over the primary trading venue. A loose definition of "same derivative contract" would promote the trading of lookalike contracts in jurisdictions with soft applications of the rules, causing market fragmentation and a regulatory race to the bottom, undermining MiFID II.

Specifically, small changes in lot size, settlement date, etc. do not make one contract meaningfully different from another, and this should be reflected in ESMA's definition of 'same commodity derivative' by adding further elements to the list in RTS 30 Article 4.

Q208. Do you agree with the proposed draft RTS regarding the procedure for the application for exemption from the Article 57 position limits regime?

We agree that any use of exemptions should be based on ex-ante authorization to do so.

7.4. Position Reporting (ITS 31)

Q210. Do you agree with the reporting format for CoT reports?

The reporting format is good but could be further improved.

By and large, the reporting format is adequate, showing the different categories of participants and the nature of their activity. The transparency of the current proposal must be maintained and strengthened. It is essential to preserve the distinction between commercial and non-commercial positions and, within the commercial subset, between risk-reducing and non-risk reducing positions. It is also crucial to post gross positions, rather than net positions, which provide little transparency. Both of these are present in the proposal, and should remain in the final version.

However, there are several areas in which the proposed format should be improved. First, a distinction is drawn in the Level 1 text between spot month contracts and contracts in other months. This should also be reflected in the CoT reports.

Second, the CFTC CoT contains several supplementary reports, including a report dedicated entirely to Commodity Index Trading. This particular form of non-commercial trading has been demonstrated to have particularly damaging effects on commodity markets when present in large volumes (e.g. Singleton 2010). Therefore, additional transparency is necessary for this sub-class of non-commercial trading.