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Directorate General Internal Market and Services

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Mr Steven Maijoor
Chair, ESMA
103 Rue de Grenelle
75007 Paris
France

Dear Mr Maijoor,

On behalf of Commissioner Barnier, I would like to thank you for your letter of 14 February, in which you draw the Commission's attention to the existence of inconsistent approaches to the application of the definition of 'financial instruments' under Directive 2004/39/EC (MiFID) with regard to certain derivatives, and the resulting negative effects on the consistent application of Regulation (EU) No 648/2014 on OTC derivatives, central counterparties and trade repositories (EMIR).

I share your view that it is essential to have a fully consistent transposition throughout the Union of the relevant MIFID provisions defining derivatives contracts, in particular to avoid the negative effects caused by any inconsistent application of EMIR. In this regard, foreign exchange forwards ('FX forwards') are contracts listed in point (4) of Section C of Annex I to MIFID. Therefore, they fall within the scope of MIFID and consequently also of EMIR.

Your letter identifies a lack of clarity about the precise delineation between FX forward contracts and currency spot contracts under MIFID. I agree with the important need for clarity and consistency in this regard and can inform you that DG MARKT will urgently assess the options for action to ensure consistent application of the legislation. Article 4(2) MIFID already empowers the Commission to clarify the definitions in Article 4 through the adoption of a delegated act, in order to take account of developments on financial markets, and to ensure the uniform application of the Directive.

I would like to share some preliminary views with you which should guide DG MARKT's assessment of this issue.

The delineation between derivative and spot contracts should be clarified, as was already the case for commodity contracts¹. In this regard, DG MARKT will need to carefully consider which delivery periods are appropriate in the FX forwards market. In order to assess the divergent application of the relevant provisions across the Union, I would be grateful if you could provide us with details of how point (4) of Section C of Annex I to MIFID and the definition of an 'FX forward' has been transposed by the national competent authorities. It would also be helpful if you could provide me with further details of the commonly accepted delivery period for currencies in the Member States and the developments in the foreign exchange markets since the implementation of MIFID.

I should also note that as the notion of 'the commercial purpose' of the conclusion of a derivative contract is only foreseen as a criterion for physically settled commodity derivative contracts in point (7) of Section C of Annex I to MIFID, it cannot be introduced for the purposes of point (4) of Section C of Annex I to MIFID as suggested in your letter.

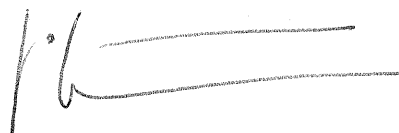
With regard to the definition of commodity forwards that can be physically settled, I can inform you that this issue was discussed during the MIFID II negotiations. The European Parliament and the Council agreed to empower the Commission to further specify in a delegated act the derivative contracts referred to in point (6) of Section C of Annex I to MIFID II that must be physically settled, taking into account specific wording included in recital 8b of MIFID II. Against this background, it would be inappropriate for the Commission to prejudice the imminent work on the delegated acts for MIFID II by developing level 2 proposals under the current MIFID, the preamble of which does not contain specific recitals to frame the definition.

I would therefore like to invite ESMA, as a part of its preparation for its advice to the Commission under MIFID II, for which you will receive a mandate before the summer, to also assess the status of physically settled commodity forwards. In addition, and in order to ensure the common, uniform and consistent application of MIFID, ESMA could also consider issuing guidelines in accordance with Article 16 of Regulation (EU) 1095/2010. I understand that ESMA has already undertaken preliminary work in this direction.

I would like to highlight that Member States are required to transpose and apply Union law. Similarly, national competent authorities are required to enforce that legislation. The transposition of MIFID has already been done by Member States, therefore only once changes are introduced in the MIFID legal framework through delegated acts those transpositions should be modified.

DG MARKT officials will be in touch with ESMA staff with regard to your kind offer to provide technical assistance in this matter.

Yours sincerely,



Jonathan Faull

¹ Article 38(2) of Commission Regulation (EC) No 1287/2006.