

#### Carbon market oversight



A tailor made regime for spot carbon trade

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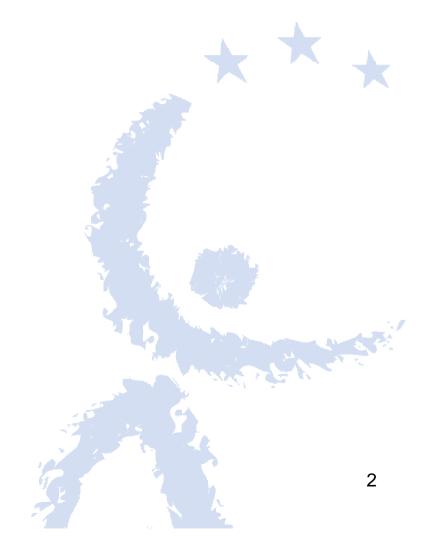
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# A tailor-made regime for spot carbon trade

- Possible modalities
- "The REMIT route"
- Questions





### Possible modalities (1)

- MiFID and MAD apply to spot secondary trade in EUAs, but the latter are not classified as financial instruments
- A regulatory system built from scratch for the purposes of the spot secondary trade in EUAs
- 3. A combination of approaches outlined under points 1 and 2



### Possible modalities (2)

#### [Option 1] Extension of the scope of MiFID and MAD without classification

- Legal form: part of MiFID/MAD amendments scope provisions of MiFID and MAD changed to stipulate direct application of their provision to secondary spot trade in EUAs
- Emission allowances and other ETS compliance units are not classified as financial instruments
  - This approach was used in the Auctioning Regulation
- Some more flexibility in disapplying the MiFID/MAD rules if that is necessary to accommodate the specificities of the ETS market
- Application of EU legislation cross-referring to MiFID's concept of financial instrument would be avoided
  - However, AML Directive would apply to intermediaries regulated under MiFID when dealing with their clients



# Possible modalities (3)

#### [Option 1] Extension of the scope of MiFID and MAD without classification (cont'd)

- Intermediation in spot carbon trading would be an investment service
- ALL exchanges trading spot EUAs would need to be authorised and supervised
- ALL intermediaries would have to obtain an authorisation and be supervised
- ETS operators dealing on own account in emission allowances would <u>not</u> be required to obtain authorisation
  - "Dealing on own account" must be ancillary to the main business
  - > ETS operator is not part of a financial group
- Transactions between two ETS operators concluded on a bilateral basis would be exempt from MiFID



#### Possible modalities (4)

#### [Option 2] A regulatory system built from scratch

- Legal form: a new, separate instrument
- New rules to be developed and agreed on issues such as:
  - taking up and pursuit of activity of intermediaries and market venues involved in the spot trading of emission allowances
  - prohibitions and preventive measures against market misconduct and abusive behaviour of participants in the trading of spot emissions
  - measures enhancing transparency and investor protection in the spot carbon market, including know your customer checks by intermediaries
  - supervision of the spot carbon market with adequate investigative and sanctioning powers for the competent authority (-ies)



# Possible modalities (5)

#### [Option 2] A regulatory system built from scratch (cont'd)

- The new bespoke regime would still need to ensure consistency and avoid overlap with rules already in force for the "financial" segment of the carbon market:
  - the derivatives trade on secondary markets
  - rules established under the Auctioning Regulation (based on MAD/MiFID/AML blueprint)



#### "The REMIT route" (1)

- COM proposal for Regulation on Energy Markets Integrity and Transparency (REMIT) – currently negotiated by the Council and the European Parliament
- Will establish harmonised rules against market abuse (insider dealing and market manipulation) for wholesale energy products and will introduce measures enhancing market transparency (post-trade transparency, trade data reporting etc.)
- Has been indicated by some stakeholders as the adequate instrument for enhancing carbon market oversight
- COM proposal did not include EUAs in its scope



# "The REMIT route"

- Measures under REMIT were tailored to professional players in the energy sector, typically subject to sectoral legislation and well-known to the supervisory authorities
  - carbon market has much wider and more diversified market participation
- REMIT focuses on issues of energy market transparency and prohibiting practices of insider dealing and market manipulation
  - due to EUAs' specificity in terms of issuance, dematerialized character and ease of transfer, carbon market requires more comprehensive rules and robust supervision
- Under REMIT, energy regulators would become responsible for day-to-day supervision of the market activity
  - > Some 90% of the carbon market is already subject to a supervisory framework for trade in financial instruments of (MiFID and MAD)



#### Questions

- In what ways (and why) should a bespoke regime diverge from existing MiFID/MAD approach? What additional elements should it cover?
- Trading and intermediation in spot emission allowances need specific rules? To what extent can the activity of intermediaries in the carbon market be limited to dealing in spot instruments?
- Impacts of introducing a bespoke regime for compliance costs of your organisation?