NASDAQ COMMODITIES

Q&A: PRE-TRADE TRANSPARENCY & RFQ TRADING SYSTEM

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1 Introduction

MiFIR, the Commission Delegated Regulation 2017/583 introduces a number of new requirements for trading on regulated trading venues.

One important objective of the regulation is to push more trading towards regulated trading venues and increase transparency in the market place, otherwise known as Pre-Trade Transparency (PTT).

MiFIR Art. 8. requires all trading venues to make public the current bid and offer prices and the depth of trading interests at those prices which are advertised through their systems. This includes both on and off-order book transactions ("block trades"), when trading is conducted under the trading venue rules.

MiFIR Art. 9 introduces a number of waivers from fulfilling PTT, such as waiver for Large In Scale (LIS) transactions, transactions in illiquid markets (IL) and package transactions, waivers that Nasdaq Oslo ASA ("Nasdaq") has applied for and received.

The regulatory technical standards on transparency requirements for trading venues and investment firms in respect of bonds, structured finance products, emission allowances and derivatives («RTS 2») sets out the methodology for calculating LIS thresholds and determining which markets are liquid.

Nasdaq has in this regard adapted its trading system and introduced a Request for Quote Trading System (RFQS) and configured appropriate parameters by introducing a new set of LIS thresholds for its liquid markets, in accordance with the regulation. The RFQS and the new parameters will be effective as of January 2nd 2020, which is in line with the ESMA Supervisory Briefing[1] published on June 3rd, 2019.

This Questions and Answers document serves for information purposes only, and should not be regarded as legal advice.

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[1] https://www.esma.europa.eu/sites/default/files/library/esma70-156-835_supervisory_briefing_pretradetransparency_non-equity_instruments.pdf

2 Questions and Answers on Pre-Trade Transparency

Q1: What is the background for introducing new rules for Pre-trade Transparency?

A1: With the implementation of MiFID II/MiFIR, a new set of requirements for Pre-trade Transparency ("PTT") became relevant for Non-Equity markets from January 3rd 2018. According to MiFIR Article 8 (1), "*Market operators and investment firms operating a trading venue shall make public current bid and offer prices and the depth of trading interests at those prices which are advertised through their systems*". As a result, all orders in non-equity markets (which includes commodity markets) have to become transparent before concluding a transaction.

The requirement is also applicable for pre-arranged transactions ("block trades") reported to Nasdaq Oslo ASA ("Nasdaq").

Q2: What does this mean in practice for block trades?

A2: In practice this means that block trades cannot be reported to Nasdaq unless it fulfills PTT or qualify for a PTT waiver or can be reported under an exemption.

Q3: What are the waivers/exemptions to this rule?

A3: MiFIR Article 9 introduces a number of "waivers" from the Article 8 requirements. This allows the local FSA's to waive the obligation for PTT when specific criteria has been fulfilled, which is the following;

- Orders that are **large in scale** compared with normal market size and orders held in an order management facility (i.e. "<u>**LIS waiver**</u>")
- Actionable indications of interest in request-for-quote and voice trading systems that are above a **size specific to the financial instrument** (i.e. "<u>**SSTI waiver**</u>")
- Derivatives which are not subject to the trading obligations specified in Article 28 and other financial instruments for which there is **not a liquid market** (i.e. "<u>**Illiquid waiver**</u>")
- Orders for the purpose of executing an **exchange for physical** (i.e. "<u>**EFP waiver**</u>")
- **Package orders** that meet one of the following conditions;
  - at least **one of its components** is a financial instrument for which there is **not a liquid market**, unless there is a liquid market for the package order as a whole (i.e. ("<u>**Illiquid market package waiver**</u>");
  - at least **one of its components is large in scale** compared with the normal market size, unless there is a liquid market for the package order as a whole (i.e. "<u>**LIS package waiver**</u>");
  - all of its components are executed on a request-for-quote or voice system and are **above the size specific to the instrument** (i.e. "<u>**SSTI package waiver**</u>").

Nasdaq has applied and received all the above-mentioned waivers from the Norwegian FSA.

In addition, MiFIR Article 8 (1) last paragraph stipulates that "…*publication obligation does not apply to those derivative transactions of non-financial counterparties which are objectively measurable as reducing risks directly relating to the commercial activity or treasury financing activity of the non- financial counterparty or of that group.*".[2]

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[2] https://www.esma.europa.eu/sites/default/files/library/esma70-872942901-35_qas_transparency_issues.pdf

What this means in practice is that, if one counterparty to the block trade is a non-financial counterpart [3] and is objectively measurable as reducing risks (i.e. hedging), the block trade is exempted from PTT.
For trades fulfilling these requirements, block trades can be reported as **Trade Type 15**, "Non-Financial Counterparty".
It is however required to apply the Risk Reducing Indicator flag for the non-financial counterpart performing a hedge at submission of the block trade to Nasdaq.

Q4: With all the waivers in place, do we still have a challenge to continue with "business as usual"?

A4: Yes. For markets deemed liquid, the minimum size of a block trade will be extensively higher than it is today. For block trades in a liquid market, the trade has to be of a certain size to be accepted, i.e. above the LIS threshold. The minimum block trade size parameters for liquid contracts will be adjusted accordingly, and trade below the LIS will be subject to PTT, unless the trade qualifies for a PTT waiver, hedge exemption or the orders to the trade are made pre-trade transparent. The latter can be solved through the new Request for Quote Trading System (RFQS), which is explained in more detail below.

Q5: Who decides the pre-trade transparency thresholds for liquid markets and which markets are affected?

A5: ESMA is on an annual basis producing pre-trade transparency calculations for liquid markets. These are available on ESMAs homepage here: https://www.esma.europa.eu/policy-activities/mifid-ii-and-mifir/transparency-calculations. In respect of listed products on Nasdaq, the PTT calculations from ESMA says the following;

Market	Delivery/Cash Sett. Location	TTM 0 – 1M[4]	TTM 1M - 1Y	TTM 1Y - 2Y	TTM 2Y - 3Y
German Power DE/AT (BL)	10Y1001A1001A63L	€ 500 000	€ 700 000	€ 1 500 000	N/A
Nordic Power (BL)	10Y1001A1001A91G	€ 500 000	€ 500 000	€ 500 000	N/A
French Power (BL)	10YFR-RTE------C	€ 500 000	€ 900 000	N/A	N/A
Spanish Power (BL)	10YES-REE------0	N/A	€ 1 000 000	N/A	N/A
Italian Power (BL)	10YIT-GRTN-----B	€ 500 000	€ 600 000	N/A	N/A
TTF	N/A	€ 500 000	€ 500 000	€ 500 000	€ 500 000
NBP	N/A	€ 500 000	€ 500 000	€ 500 000	€ 500 000

Please note that EUA's does not have maturity buckets. ESMA has given EUA's a fixed number of Tons of Carbon Dioxide equivalent to 100 000 tons, which is equivalent to 100 lots at Nasdaq.

As the thresholds are in Euros, Nasdaq has decided to convert the numbers to fixed lot values. These can be located in the Nasdaq Commodities Market Model, located in the Resource Center section on the Nasdaq Commodities web here; https://www.nasdaq.com/solutions/power-derivatives-european-commodities.

Please see Appendix 1 below for more details.

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[3] Non-Financial Counterpart as defined under EMIR

[4] TTM = Time to maturity, M = Month, Y=Year

3 Questions and Answers on Request for Quote Trading System

Q6: Why have you introduced the Request for Quote Trading System (RFQS)?

A6: The main reason for introducing the RFQS is to comply with MiFIR Art. 8 on pre-trade transparency for orders that are below LIS for which there is a liquid market. To ensure that Nasdaq fulfils its obligations, the need for a tool for this purpose was required.

Q7: How will RFQS comply with MiFIR Art. 8?

A7: The RFQS is designed in accordance with RTS 2 Annex I[5], which is a trading system where a quote or quotes are provided in response to a request for a quote submitted by one or more other members or participants. The quote is executable exclusively by the requesting member or market participant. The requesting member or participant may conclude a transaction by accepting the quote or quotes provided to it on request. The quotes and the attaching volumes from any member or participant which, if accepted, would lead to a transaction under the system's rules. All submitted quotes in response to a request for quote may be published at the same time but not later than when they become executable.

The RFQS enables Exchange Members to initiate private RFQ's, through so-called Directed Quote Requests (DQRs), and conclude transactions within the RFQ trading system on a private and anonymous basis, in line with the description set forth in RTS 2 Annex I.

Pre-trade transparency is fulfilled by the exchange publishing all quote responses to a RFQ in a public order book, no later than when they become executable. The public order book will be available in Nasdaq's market data feeds and in the native trading front-end, Trading Workstation from January 2nd 2020. The public order book will also be available on Nasdaq's market prices web page[6] in early January 2020.

Q8: Who can use the RFQS?

A8: The RFQS can be used by all Exchange Members, and will be enabled for all as of January 2nd 2020. Exchange members' current appointments towards Block Broker Members will also enable Block Broker Members to facilitate private RFQ's as on-behalf service.

Q9: Does this mean that I have to conclude a trade in the RFQS, if my order via a broker is below the LIS and does not have a waiver or fall under an exemption?

A9: Yes. Nasdaq as a regulated trading venue have to show pre-trade transparency for all orders done under the "system rules". The current block trades are concluded under Nasdaq's rulebook, hence under the "system rules". This makes all orders subject to the PTT regulation.

Q10: How do I conclude a below LIS trade in the RFQS with assistance from a block broker member, and is the process manual or automatic?

A10: First of all you need to appoint the relevant block broker member, authorizing it to facilitate private RFQ's. The block broker members that you has already appointed for reporting of block trades will automatically be enabled to perform private RFQ's on your behalf.
Secondly, the broker will facilitate the private RFQ to be sent to relevant respondents that are willing to give a

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[5] https://ec.europa.eu/finance/securities/docs/isd/mifid/rts/160714-rts-2-annex_en.pdf

[6] http://www.nasdaqomx.com/commodities/market-prices/transactions (Under section "Commodities RFQ")

quote (one or several).

Thirdly, you will have to accept the incoming quote from the respondent(s) in order to conclude a trade. If no quote response is accepted, the private RFQ will expire and not result in a trade.

Please note that the RFQ process via brokers has been designed with automatic execution. This means that Exchange Members will be given a limited time of 15 seconds to void a quote request or quote response, registered by the broker. If not voided, the quote response and/or matching quote accept will be executed automatically by the RFQ trading system, on-behalf of the participants involved in the private RFQ.

Q11: Where will I see; sent quote request, sent quote responses and received quote responses?

A11: The native trading front-end, Trading Work Station (TW)[7], has been enhanced with several new windows where you can see all activity related to RFQS. Please make sure you have the latest version of TW, and have a look in the updated user guide under the following topics; "Directed Quote Request Window: Sent Request", "Directed Quote Request Window: Market Maker"; "Directed Quote Request Window: Responses"-

The Q-port application has also been upgraded with RFQS, with a new window called "Directed Quote Request", where users can monitor the RFQ process, submit, respond and cancel private RFQ's.

Q12: Which instruments are available in the RFQS?

A12: All instruments listed in the regular order book is available in the RFQS, as of January 2nd 2020.

Q13: Is it possible to trade above the LIS in the RFQS, and will above LIS orders become public in the public order book?

A13: Yes, if the order is above the LIS thresholds, and processed in the RFQS, the orders will become public (PTT) in the public order book.

Q14: If orders above LIS processed in the RFQS is published pre-trade, will regular block trades above LIS also become transparent before execution?

A14: No, all block trades above LIS will only be subject to post trade transparency, as it is today.

Q15: Is the RFQS exclusively available in your native interfaces?

A15: The system is available over the OMnet and FIX API, and ISV's may connect and process private RFQ's, using their own front-ends.

Q16: Is there any added cost to use the RFQS?

A16: No. Exchange Members with access to the regular order book will have access to RFQS without any additional cost. Block Broker Members with access to Q-port will have access to RFQS through this interface, and do not need to apply or buy additional access to facilitate private RFQ's for other Exchange Members.

Q17: How can I tell the difference between a RFQS trade and a regular order book trade?

A17: Trades from the RFQS will be marked with the market model typology flag "RQ".

Q18: What will be the RFQS opening hours?

A18: The RFQS will be open during the same period as the regular order book.

Q19: In case of a broker assisted private RFQ, will I be able to view the time of when a response was received by the broker?

A19: Yes. The broker will register an "Initiation time", to show the market when a firm quote response was received, as there will be a short time-lag from when the broker received the firm quote response until it is registered in the RFQS. Brokers and Exchange Members must ensure that the price of any quote response represents the "fair market value price" for that trade, defined as the price considered to be the best available for a trade of that size and kind at that time.

Q20: Will trades concluded in the RFQS be included in the determination or calculation of the daily fix?

A20: No. Prices of RFQS concluded trades will not be included in the determination or calculation of any Daily Fix.

Q21: When using a broker to facilitate private RFQ's, do I pay an extra fee?

A21: When concluding a trade in the RFQS, regular trading fee applies. However, in case you use an approved brokers, Nasdaq will refund incurred trading fee on a monthly basis. We hope to make this process better in the near future, where assisted RFQS will have a different trading fee versus initiating private RFQS directly yourself. Regular clearing fees do however apply, as per any other order book or off-order book trade.

Q22: Is it possible to have several RFQ's open at the same time for the same instrument series?

A22: No. One Exchange Member can only have one RFQ open for the same instrument series at the time. When the lifetime of the RFQ has expired, the Exchange Member may open a new RFQ. It is though possible to have several RFQ's open at the same time, in different instrument series.

4 Appendix 1 – LIS thresholds and liquid maturities

Contract type	LIS in €	LIS in lots	Liquid Maturities
Nordic Days	€ 500 000	726	All
Nordic Week	€ 500 000	104	All
Nordic Month	€ 500 000	24	All
Nordic Quarter	€ 500 000	8	All
Nordic Year	€ 500 000	2	First 2 years
Italian Power Base Day	€ 500 000	465	All
Italy Power Base Week	€ 500 000	67	All
Italian Power Base Working Day Week	€ 500 000	93	All
Italian Power Base Weekend	€ 500 000	233	All
Italian Power Base Month	€ 600 000	18	All
Italy Power Base Quarter	€ 600 000	7	First 4 quarters
Italian Power Base Year	€ 600 000	2	First year
German-Austrian Power Base Day	€ 500 000	677	All
German-Austrian Powe Base Week	€ 500 000	97	All
German-Austrian Powe Base Month	€ 700 000	31	All
German-Austrian Power Base Quarter	€ 700 000	11	All
German-Austrian Powe Base Year	€ 1 500 000	6	First 2 years
Spanish Power Base Week	€ 1 000 000	135	From 4th week
Spanish Power Base Month	€ 1 000 000	31	All, except front month
Spanish Power Base Quarter	€ 1 000 000	11	First 4 quarters
Spanish Power Base Year	€ 1 000 000	3	First year
UK GAS Day	€ 500 000	1	All
UK GAS Working day week	€ 500 000	3	All
UK GAS Weekend	€ 500 000	6	All
UK GAS Balance of Working day week	€ 500 000	3	All
UK GAS Balanace of month	€ 500 000	1	All
UK GAS Month	€ 500 000	1	All
UK GAS Quarter	€ 500 000	1	All
UK GAS Season	€ 500 000	1	All
UK GAS Year	€ 500 000	1	First 3 years
Dutch GAS Day	€ 500 000	1 429	All
Dutch GAS Working day week	€ 500 000	286	All
Dutch GAS Working day Weekend	€ 500 000	715	All
Dutch GAS Balance of working day week	€ 500 000	358	All
Dutch GAS Balanace of month	€ 500 000	47	All
Dutch GAS Month	€ 500 000	47	All
Dutch GAS Quarter	€ 500 000	16	All
Dutch GAS Season	€ 500 000	8	All
Dutch GAS Year	€ 500 000	4	First 3 years
French Power Day	€ 500 000	491	All
French Power Weekend	€ 500 000	246	All
French Power Working day week	€ 500 000	99	All
French Power Week	€ 500 000	71	All
French Power Month	€ 900 000	29	All
French Power Quarter	€ 900 000	10	First 4 quarters
French Power Year	€ 900 000	3	First year

Note to LIS conversion

Article 13 - 9 of RTS 2 states that Market Operators may convert the trade sizes determined according to paragraph 2 to the corresponding number of lots as defined in advance.

The Questions and Answers On MiFID II and MiFIR transparency topics[8] published by ESMA states in answer to question 19 on Non-equity transparency topics that the threshold in Lots shall be converted using the below formula for futures:

$$\text{Threshold in lots} = \frac{\text{notional value of the threshold}}{\text{Lot size} * \text{Arithmetical average closing price of the underlying}}$$

Where the notional value is the notional value in the trading currency of the derivative contract, the lot size is the contract size (price multiplier in the case of index futures/forwards) determined by the trading venue for that derivative contract and the arithmetical average closing price of the underlying is determined by the value resulting from the average of the available closing prices of the underlying (or, when not available, the reference value determined by the relevant market of the underlying) during the 12-months of the previous year. In all cases, the threshold in lots resulting from the division shall be rounded to the minimum tradable number of lots for orders. The value can be rounded up or down, but the type of rounding shall be determined by the end-value that is closer to the pre-rounding value.

Nasdaq Commodities are converting the LIS sizes in EUR for all relevant sub-classes as determined by ESMA to a number of lots using the above following formula:

Where

- Lot size= Price Quotation Factor[9]
- Arithmetical average closing price of the underlying=Average daily FIX on the underlying over the previous year[10].
- For sub-classed denominated in other currencies than EUR the ECB rate for the last day of the determination period is used.

Nasdaq has rounded up the lot values to the nearest whole number.

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[8] https://www.esma.europa.eu/sites/default/files/library/esma70-872942901-35_qas_transparency_issues.pdf

[9] Number of hours or therms in the applicable series.

[10] 2016 numbers used, as the liquidity assessment for the current LIS values by ESMA is for 2016. Update expected on April 30 2020, according to RTS 2, Art. 13 (17), with effective date 1 June 2020.