

LONDON NOTICE NO. 3695

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POSITION MANAGEMENT REGIME FOR LONDON COMMODITY CONTRACTS – CONFIRMATION OF ARRANGEMENTS AND INCREASE TO DELIVERY LIMIT AND DELIVERY LIMIT EXEMPTION FOR THE WHITE SUGAR FUTURES CONTRACT

Executive Summary

In response to Member feedback, this Notice confirms certain elements of the Position Management Regime for London Commodity Contracts. In addition this Notice informs market participants of an increase to the Delivery Limit and Delivery Limit Exemption for the White Sugar Contract, effective from the May 2013 delivery month onwards.

1. Introduction

- 1.1 London Notice No. [3635](#), issued on 13 September 2012, set out the procedures and associated guidance in relation to enhancements to the Exchange's Position Management Regime for London Commodity Contracts ("the Contracts"), including the introduction of Accountability Levels, Delivery Limits and Delivery Limit Exemptions. The enhanced regime became effective from the following delivery months onwards: November 2012 for Robusta Coffee Futures; December 2012 for Cocoa and White Sugar Futures and January 2013 for Feed Wheat futures.
- 1.2 The Exchange has now conducted a review of how the enhanced regime has operated since its introduction and has listened to the feedback it has received from market participants. Consequently, the Exchange believes it would be helpful to confirm certain aspects of the regime. Furthermore, for the reasons outlined later in this Notice, the Exchange has determined to increase the Delivery Limit and Delivery Limit Exemption in respect of the White Sugar Futures Contract from the May 2013 delivery month onwards. It should be noted that no change is being made to the limits/levels that apply to the other London Commodity Contracts.

2. Position Management Activities

- 2.1 London Notice No. [3635](#) sought to make clear that the Exchange's day-to-day position management activities continued, notwithstanding the introduction of the more prescriptive elements of the regime (i.e. Accountability Levels, Delivery Limits and Delivery Limit Exemptions).
- 2.2 A number of market participants have reported that they had interpreted the introduction of Delivery Limits as meaning that any market activity where the associated positions were beneath the Delivery Limit would be allowed to continue unfettered, without the need for the Exchange to seek explanations for the rationale for such positions, or otherwise to intervene. The Exchange

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wishes to make clear that its obligation to maintain a fair and orderly market stands in all circumstances; it must therefore reserve the right to scrutinise any market activity in the interests of the market as a whole and market participants can be expected to respond to Exchange queries at any time regardless of the size of position held on the market.

- 2.3 This is particularly pertinent in the current environment where levels of certified stocks in Robusta Coffee and Cocoa are at historically low levels. As market participants will be aware, in its management of Robusta Coffee and Cocoa positions, the Exchange must take into account a wide range of factors in respect of each Contract including, but not limited to: the overall level of Open Interest; the individual positions that are held by market participants; the overall level of certified stocks; and the certified stocks that are held by each position holder. The Exchange uses these factors (alongside other relevant external factors, where applicable) to determine whether tensions may arise or have arisen, i.e. whether there is any dominant position that may have or is having an adverse impact on the market. The characteristics of dominant positions will vary depending on the exact circumstances in questions. However, it is clear that a long position holder who holds a significant percentage of the total Open Interest and/or a long position holder who also holds a significant percentage of certified stocks will attract greater scrutiny from the Exchange.
- 2.4 An inevitable consequence of these lower certified stock levels is that a market participant's certified stock holding has a greater potential to represent a significant percentage of the overall level of certified stocks. The Exchange has a regulatory obligation to maintain a fair and orderly market, and, where a dominant position-holder exists, the management of that position will be closely monitored by the Exchange to ensure that any price movement in the relevant contract is in accordance with the Exchange's regulatory obligations. In practice this may result in the Exchange requesting that a dominant position-holder provide liquidity to the market up to a pre-defined limit based upon the spread between the front and second delivery months. Such a request may require a dominant position-holder to reduce the size of their position to a certain level or may be a general request to provide liquidity up to the agreed spread level dependent upon market circumstances.

3. Delivery Limit Exemptions

- 3.1 In response to feedback it has received from market participants, the Exchange wishes to reconfirm the procedures in respect of Delivery Limit Exemptions.
- 3.2 London Notice No. [3635](#) described the four Delivery Limit Exemption types ("Cash and Carry", "Short Financing", "Physical Off-Take" and "Stock Holder" Exemptions) and the requirements in relation to each Exemption type. For the avoidance of doubt:
- (a) in relation to Physical Off-Take and Stock Holder Exemptions, the Member is required to proceed with the relevant delivery for the full amount of the Exemption level granted; and
 - (b) in relation to Cash and Carry and Short Financing Exemptions delivery is not required in the specific circumstances set out in London Notice No. [3635](#).

4. White Sugar Futures

- 4.1 During the consultation process, the Exchange provided market participants with the opportunity to comment on its proposals for the enhanced regime, including requirements in respect of Delivery Limit Exemptions. The Exchange noted the responses from a small number of White Sugar market

participants, which were largely predicated on the fact that White Sugar is a Free on Board (“FOB”) contract and that White Sugar taken for delivery cannot subsequently be redelivered. As a result of those responses, the Exchange explored whether it would be desirable to tailor certain aspects of the regime for the White Sugar market.

4.2 On balance, the Exchange determined that:

- (a) White Sugar should indeed be subject to Delivery Limits, given the regulatory developments at European Level;
- (b) in relation to the arrangements for Delivery Limit Exemptions, any move to allow so-called “optionality” in respect of a granted Physical Off-Take or Stock Holder Exemption would largely make meaningless the base Delivery Limits;
- (c) however, the 5,000 lot Delivery Limit for Sugar should nonetheless accommodate all legitimate commercial business.

4.3 The Exchange has now received further feedback from market participants who have reported that the White Sugar Delivery Limit level, combined with a lack of optionality in respect of Exemptions may have acted to unnecessarily constrain legitimate commercial business, particularly because of the delivery intentions expressed by certain market participants in the December 2012 Delivery Month. Whilst the Exchange understands that some market participants would favour the introduction of optionality in order to resolve this issue, it considers that such a fundamental change, bearing in mind the objectives behind the design of the enhanced regime, needs to be considered thoroughly and in conjunction with market participants. However, in order to secure the Exchange’s primary objective, of ensuring that its commodity contracts permit all legitimate commercial business, the Exchange has determined to increase the White Sugar Futures Delivery Limit to **10,000 lots** and the Delivery Limit Exemption to **15,000 lots** with effect from the May 2013 delivery month. As a result, the Accountability Level will be 10,000 lots in respect of the front delivery month and 20,000 lots in respect of any deferred delivery month.

4.4 The Exchange will shortly begin to re-engage with White Sugar market participants in order to hear their views on the appropriate long term approach in respect of this Contract and its delivery requirements.

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