

To: All members and other interested parties

Ref: 22/145

Classification: Consultation General

Date: 13 May 2022

Subject: **Consultation on OTC Position Reporting for all Physically Deliverable Metals & Accountability Levels for Reportable OTC Positions**

Summary

1. The London Metal Exchange (“**LME**”) seeks the views of Members and other interested parties on the following proposals, which the LME believes will further enhance its visibility of OTC markets in the near term, in the interests of the market as a whole: (i) the introduction of a revised requirement for Members to report all OTC positions in physically deliverable aluminium, aluminium alloy, cobalt, copper, lead, NASAAC, nickel, tin and zinc to the LME on a weekly basis with no minimum position size threshold (noting that should the LME adopt this proposal, it intends to withdraw the existing daily nickel-related OTC position reporting requirements set out in Notice 22/064); and (ii) the extension of Accountability Levels to OTC positions (each a “**Proposal**” and together the “**Proposals**”). This Notice also lays out the LME’s current view on the longer term plan to establish a systematic OTC trade and position reporting framework that will assist in improving future market transparency and stability.

Defined terms

2. Defined terms used in this Notice shall have the meaning ascribed to them in the Rules and Regulations of the LME (the “**Rulebook**”) or the Policy Relating to Position Management Arrangements (the “**Policy**”) unless otherwise defined in this Notice.

Background

3. In recent years, the LME has had dialogue with Members and other interested parties regarding the need for more visibility of OTC dealings in metals. The LME has regulatory obligations, amongst other things, to monitor, detect and investigate instances of potential market abuse, and to ensure the fair and orderly operation of its market. Proposals to expand the scope of the LME’s visibility over OTC markets, in particular proposals relating to the introduction of OTC reporting in respect of LME metals, have previously been met with resistance from certain market participants. In 2020, the LME introduced certain powers to request information about OTC dealings in metals: a number of concerns were raised by Members during and after that consultation process¹ and consequently, the LME conceded in the decisions flowing from this consultation that these powers would be relatively limited in their application, and that they would primarily be used in circumstances where the LME has genuine, reasonably held grounds for suspecting that market abuse either may be occurring, or has occurred, on its market. Use of these powers is therefore limited, and requires a relatively high evidential bar to first be met. The Discussion Paper on Market Structure published in January 2021, and the corresponding Response Paper published in March 2021², detailed the potential benefits of receiving regular OTC data to enable the LME to monitor OTC trading in instruments linked to the LME. Given some market participants remained unsupportive of this view, the Response Paper confirmed that the LME would investigate the need to report OTC trading and position data on contracts similar to LME contracts; however, the LME was also cognisant of the need to

¹ See LME Notices 20/182, 20/183, and 20/217.

² Relevant documents are available at <https://www.lme.com/Trading/Initiatives/Market-structure-evolution>.



explore such changes sensitively and, given market feedback, considered any potential enhancements to reporting a longer-term objective.

4. Recent events in the LME Nickel market have demonstrated the effects that OTC activity can have on the wider LME market. Therefore in order to: (i) improve the ability of the LME to oversee activity holistically through increased visibility; (ii) ensure future market stability; and (iii) ensure continued compliance with its regulatory obligations, the LME exercised its available powers to require OTC position information in relation to Nickel positions. Further, the LME believes it is now essential to accelerate the introduction of regular OTC reporting, and correspondingly to introduce related Accountability Levels, for all physically deliverable metals on the LME.
5. In Notice 22/064, as an interim measure, the LME required Members to submit certain nickel-related OTC position data on a daily basis. Subsequently, in Notice 22/099, the LME set out its intentions to extend OTC position reporting requirements to other metals in the short term, while also signalling its view that, in the longer term, the LME considers that it may be appropriate, and in the interests of the market as a whole, to capture near-real time reporting of OTC trades alongside OTC position reporting.
6. Against this background, this Notice sets out new OTC position reporting requirements which the LME believes it is appropriate to introduce for all physically deliverable metals on the LME. Given the decisions taken in previous consultations (due to push-back by participants as detailed in paragraph 3), the LME considers that it is appropriate to consult on the introduction of these new requirements. This Notice also sets out the LME's current view on a longer term OTC reporting framework.
7. For the avoidance of doubt, in addition to the measures set out in this Notice, the LME will continue to proactively develop and assess further potential market structure reform proposals aimed at mitigating the risk of circumstances similar to those leading to the events of 8 March 2022 arising in the future on the LME (details regarding the LME's current thinking on longer-term OTC reporting are outlined in paragraphs 31-34 below). Where the LME considers it to be in the interest of the long-term health, efficiency and resilience of the market and appropriate to do so, the LME may seek to proactively introduce further such measures prior to the conclusion of the ongoing Independent Review, and will subsequently assess any further appropriate changes in light of the findings in the Independent Review.

Consultation process, timing and steps following this consultation

8. This consultation is open to all interested parties, including (without limitation) Members and their clients, and other interested parties. Responses must be submitted in writing, as set out in paragraph 9 below. The consultation will remain open for responses until **18:00 London time on Friday 27 May 2022**. The LME acknowledges that this period is shorter than the consultation period that the LME typically adopts in relation to consultations. However, the LME considers a two-week period to be sufficient and proportionate in light of: (i) the limited nature of the Proposals; and (ii) the LME's urgent need to ensure that it has a clear understanding of activity that could impact on the orderly functioning of the LME's metals markets, during the current period of global uncertainty and supply chain pressures. Further, in the interests of ensuring a level playing field between respondents to the consultation, the LME shall not consider responses submitted after the deadline.
9. Any questions regarding this consultation, and any formal written responses, should be submitted by email to consultation@lme.com.
10. The LME may need to share responses with regulatory authorities, members of its group, and its legal or other professional advisors, or as required by law. Anonymised responses (verbatim or paraphrased) may be included in any Notice(s) relating to this consultation. Apart from this, all responses will be treated in confidence.
11. Following due consideration of any responses and following the close of this consultation, the LME may implement:
 - (a) in respect of any or all of the Proposals, that Proposal, a modified version or alternative of that Proposal, or no measures in respect of that Proposal;
 - (b) any other measure(s); or
 - (c) no measures.



12. Following this consultation and any necessary regulatory engagement, the LME may advise Members and other market participants via one or more Notices of when any decisions relating to the Proposals shall take effect. For completeness, an indicative timeline is set out in paragraph 29 below.

Weekly OTC position reporting Proposal

13. In developing the weekly OTC position reporting Proposal set out in this section of the consultation, the LME has taken into account the anticipated benefits of regular OTC position reporting, particularly in identifying the development of significant positions and the potential consequent risks to the LME market, and balanced this against the challenges of implementing such reporting for Members in the short term. The LME proposes that the Proposal as described in paragraphs 14-23 would be given effect through a new Rule, as set out in proposed form in paragraph 24.
14. The LME considers that it is appropriate at this stage, informed by observations relating to the recent Nickel market conditions, to introduce OTC position reporting on a weekly basis across all metals that are physically deliverable on the LME, so as to provide the LME with timely visibility of significant positions in the OTC market. Alongside this, the LME considers it appropriate to expand its current powers to request ad hoc information about OTC dealings in metals to cover any situation where it judges that such data could be important for the monitoring and ongoing operation of fair and orderly markets. This would enhance the LME's ability to monitor its own market (i.e. the on-exchange market). For the avoidance of doubt, the LME intends that any implementation of this Proposal would result in the withdrawal of the existing requirement to daily report OTC nickel positions, which was introduced in Notice 22/064, but such withdrawal on a standalone basis is not the subject of this consultation. In the LME's view, the proposed weekly reporting requirement would most efficiently be operationalised as set out in the following paragraphs in this section of the consultation Notice.
15. Under this Proposal, the LME would require all Members to submit the OTC positions they hold with clients³, each Monday, in aluminium, aluminium alloy, cobalt, copper, lead, NASAAC, nickel, tin, and zinc, as of the previous Business Day's close. In the event a Monday falls on a non-Business Day, Members would be required to submit their reports on the next Business Day. Reports would be required to be submitted via email with the email subject title and file name of "XXX - LME Daily OTC Position Reporting COB DD MMM YYYY", where 'XXX' refers to the Member's mnemonic and 'DD MMM YYYY' refers to the date of the previous Business Day's close. The report would subsequently be sent to OTCpositionreporting@lme.com by no later than 14:30 London time on the relevant Business Day, as above. In the event a Member holds no OTC positions in any of the above-mentioned metals, the LME proposes that Members should confirm this with the submission of a nil file return to ensure that the information available to the LME is as complete as possible.
16. To ensure consistency in the data provided to the LME, the LME proposes that Members would be required to report using a reporting template provided by the LME. The data that the LME considers would be necessary for the purposes of enhancing its visibility of OTC positions is set out in the Annex of this Notice. The format of the file would be in Excel (.xlsx format). The template would also be made available on the LME website, with any subsequent changes to the template notified to Members and reflected in the website version.
17. The weekly OTC position reporting arrangements proposed in this consultation are intended as an interim measure, pending any further proposals brought forward by the LME in due course (considering the LME's views on longer-term reporting as laid out below, alongside any recommendations resulting from the Independent Review) regarding a longer-term OTC reporting framework. However, for the avoidance of doubt, the LME considers it appropriate for it to have the ability to adjust the frequency of the reporting requirements outlined above, including (without limitation) applying different reporting frequencies and thresholds to different metals, as appropriate and further, may revise the required reporting details set out in paragraph 19-23 below, as necessary. Given that the longer-term consultation proposals may take some time to develop, the LME may also implement further interim measures where the LME considers that they could help operationalise weekly OTC position reporting (such as setting up a mechanism to submit the data into a secure FTP server, and evolving the reporting template).
18. To ensure that the LME has appropriate powers to react to evolving and reasonably foreseeable circumstances that may require the LME to change the operational parameters of the reporting (such as

³ For the avoidance of doubt, this includes any clients, not just "Clients" as defined in the LME Rulebook.



the specific data requested, the format of this data, and the frequency of reporting etc) either on a one-off, or periodic basis should this be considered necessary, the proposed Rule set out in paragraph 24 provides the LME with a degree of flexibility to do so, without the need for further consultation (although with such advance notice as is practicable in the circumstances).

Details of positions that must be submitted

19. Under this Proposal, Members would be required to submit details of all positions in any of the metals listed in paragraph 15 above (whether the positions are financially settled against, or by reference to, an LME reference price, or physically deliverable with LME Warrants or similar instruments, e.g. warehouse receipts relating to substantially similar quality metal in a location, or locations, represented by LME warehouses) which are not cleared by LME Clear, and where the total metal to be reported represents at least 20% of the underlying. Where the metal represents less than 100% of the underlying value (such as, but not limited to, a commodity index containing a basket of metals), the LME proposes that Members should report the equivalent metric tonnes of metal delta in the 'Position' field set out in the reporting template in the Annex to this consultation Notice.
20. In order to simplify the reporting requirement, and ensure that the LME has a complete view of OTC positions, the LME proposes that no minimum threshold should be applied to reporting under this Notice (unlike the 100 lot threshold previously in place for Nickel pursuant to Notice 22/064). All positions, regardless of size, should be included within a Member's report.
21. Further, the LME proposes that when reporting in the template, for each position-holder there should be one net position for metal, OTC instrument type, prompt date, strike/option type (if relevant). All positions included in a report must be reported in metric tonnes. To avoid the LME needing to infer each Member's own OTC position, the OTC positions held by clients (including those held with a Member's affiliate – see paragraph 23) should be reported on separate rows to the OTC positions held by Members, and each position should be reported from the perspective of the position-holder.
22. In the instances where an OTC options position is reported, the LME proposes that the Member should be required to report the option position in the Position field as well as the equivalent delta futures position in the Delta Position field. The Delta Position field should correctly reflect the direction of the equivalent futures position, such as, for example, a long put option position being reflected as a short equivalent futures position.
23. Further, as noted above, the LME considers that the Member should report the ultimate beneficial owner of the metal (including where the relevant position is held between a client and an affiliate of the Member), and identify the entity by its correct legal entity name and (where applicable) the entity's LEI. The LME acknowledges that in certain circumstances, which are understood to be limited, Members may be subject to overriding legal restrictions or obligations (e.g. bank secrecy requirements) that may affect their ability to legally disclose details of ultimate beneficial owners. The LME proposes that in such instances, affected Members would be required to provide a reasoned justification to the LME, with sufficient information to enable the LME to assess the validity of the rationale.

Proposed Rule

24. The LME proposes that the Proposal described in paragraphs 14-23 above would be given effect through the introduction of the following Regulation which (if adopted) shall be reflected within the LME Rulebook as new Regulation 24 Part 2:

“PERIODIC OTC POSITION REPORTING

- 24.1 *Each Member shall provide to the Exchange, on a weekly basis (or such other frequency may be specified by the Exchange pursuant to Regulation 24.2): (i) such information in respect of positions under over-the-counter contracts; (ii) in respect of such metal(s); (iii) at such times; and (iv) in such format, as in each case shall be specified by Notice. For the avoidance of doubt, such information may include information regarding the over-the-counter positions of the Member and/or its affiliates and/or its clients.*
- 24.3 *The Exchange may, in its discretion, by Notice and with such advance notice as is practicable in the circumstances: (i) dis-apply the reporting requirement under Regulation 24.1 from any metal or, include any additional metal(s) to such reporting requirement; and/or (ii) modify the*



reporting thresholds for any metal; and/or (iii) modify the reporting format; and/or (iii) modify the reporting frequencies or timescales for submission of the information.”

Transparency considerations

25. The LME will not at this stage publish or otherwise create public transparency around the data that the LME proposes to require under the weekly nor ad hoc OTC position reporting arrangements described above. However, as set out further below, and as outlined in the Discussion Paper (January 2021) and Response Paper (March 2021), the LME continues to assess the potential benefits of wider transparency and how it may be implemented in future.

Accountability Levels Proposal

26. Further to the application in Notice 22/064 of Accountability Levels to OTC positions in Nickel, the LME proposes that the Accountability Levels set out within the LME’s Policy Relating to Position Management Arrangements (the “**Policy**”) should be extended to apply to all OTC positions reported by Members (in addition to the existing on-Exchange positions). Under this Proposal, where a Member or a client (which term would include any clients, not just Clients as defined in the LME Rulebook) has a position that is above the applicable Accountability Level, or the LME otherwise deems it appropriate at its absolute discretion, the LME may request the rationale for the position-holding, and the Member must comply with the request.
27. The LME notes that its ability within the Policy to adjust the Accountability Levels from time to time would, if this Proposal is adopted, apply to both on-Exchange and OTC positions. This would require certain textual changes to be made to paragraphs 54 to 61 of the Policy to: (i) extend the application of Accountability Levels to reportable OTC positions; (ii) clarify the application of Accountability Levels to client positions rather than to Clients as defined in the LME Rulebook; and (iii) clarify that the LME may, at its discretion, elect to consider OTC positions separately to on-Exchange positions, or net them together, for the purposes of determining if the position is in breach of the Accountability Level threshold.
28. Further, for the avoidance of doubt, the LME notes that this Proposal applies only to Accountability Levels, but does not apply to the Lending Rules or Position Limits.

Anticipated timeline for implementation of the Proposals

29. Subject to the outcome of this consultation, the LME intends to communicate its decisions in relation to the Proposals on or around 13 June 2022 and in any event, given the LME’s views on the importance of these measures for the market as a whole, the LME will communicate its decisions as soon as practicable. The LME anticipates that any measures that may be implemented as a result of this consultation would take effect on or shortly after the date on which consultation outcomes are communicated.

Consultation questions

30. Members and other interested parties are invited to provide their views on any of the matters raised in this consultation and in particular on the following consultation questions:
- Q1 Do you have any views on the Proposals set out above?
- Q2 Do you have any comments on the proposed Regulation 24, Part 2?
- Q3 The LME understands that the Proposals may have operational implications for Members. Given the current market conditions across commodity markets, the LME believes that these Proposals represent a proportionate and appropriate approach to implementation. Where Members and other interested parties accept the policy direction anticipated in this consultation Notice, do you believe that the operational processes described above represent appropriate operational means to achieving this? If you have any suggestions that you consider may assist in streamlining the Proposal processes, please provide your views.



LME view on longer term OTC information and transparency

31. The LME has long recognised the important role of OTC trading in metals markets, allowing participants to trade bespoke contracts to suit their hedging needs or trade more exotic instruments than are available on the LME's Execution Venues. However, OTC trading can also have negative impacts, including limiting the ability of the LME to oversee activity holistically, thereby reducing transparency for all participants and fragmenting liquidity. While some of these negative impacts may be unintended consequences of "positive" uses of OTC trading (e.g. a physical client undertaking a hedge trade that is not available on the LME directly), others may be as a result of purposely using OTC trades to obscure transparency from the wider market and therefore reduce oversight by the LME. The LME believes it is in the interests of the market as a whole for it to seek to reduce or help mitigate these negative aspects of OTC trading.
32. Following the events of 8 March 2022, the LME has already introduced OTC data reporting, and through this consultation Notice is consulting on enhancing these measures, in order to respond to the risks posed to the market. The LME continues to consider it important, over the long term, to develop and assess ways to increase the transparency of OTC trading in metals markets, alongside addressing other potential negative impacts of OTC trading. In the LME's view, future changes could include publishing aggregated summary data or aligning the publication of OTC trading and position data with that of LME data. In considering appropriate next steps, the LME recognises that it will need to balance relevant factors regarding the appropriate level of transparency. For example, if increased OTC transparency had the impact of significantly reducing overall trading in LME markets, then this would likely not be in the interest of the market as a whole, nor consistent with the wider regulatory direction of travel to increase trading in lit venues.
33. The LME's current view is that the approach that is most likely to be in the interests of the market as a whole (and in particular from an operational perspective) is to mandate that all OTC trades and positions must be reported. These reports should be able to be made in a way that utilises processes already in place for LME on-exchange trade booking and position reporting. For example, this could be achieved by:
 - OTC trade reporting – adding appropriate fields and identifiers to LMEsmart to allow OTC trades to be "booked" alongside Exchange trades. The LME would then be able to process these OTC trades in much the same way as it publishes Exchange trades, albeit without sending them to LME Clear to be cleared.
 - OTC position reporting – developing a daily OTC position report for Members to submit to the Exchange alongside their MiFID Commodity Position Report.
34. The LME will continue to consider the topic of OTC reporting, the best path forwards for the market, and the most appropriate timelines for implementation, subject to consultation as appropriate. While any relevant findings from the Independent Review will also be considered and factored in to the LME's plans in due course, the LME will not delay taking appropriate actions in order to wait for the outcomes of the Independent Review.

Benefits and unintended consequences

35. As noted above, the LME acknowledges that there may be operational implications for Members in complying, or otherwise in connection, with the Proposals set out in this consultation. However, subject to any views expressed in response to the consultation, the LME's current view is that the operational implications for Members in connection with the Proposals are justified, in the interests of the membership and the LME ecosystem as a whole, and will ensure that the LME continues to comply with its regulatory obligations. The LME has not identified any unintended consequences not set out in this consultation as a result of any of the Proposals. However, the LME is interested in the views of respondents to this consultation in this regard.

Tom Hine
General Counsel, LME Group

Cc: Board directors
User Committee



Annex

OTC position reporting template (Excel .xlsx)

Field Name	Business Date	Member	Position Holder Name	Position Holder LEI	Metal	Contract Type	Contract Description	Currency	Averaging From	Averaging To	Prompt	Option Sub Type	Strike Price	Position	Delta Position
Mandatory (M), Optional (O), Conditional (C)	M	M	M	C	M	M	C	M	C	C	M	C	C	M	C
Description	Date positions are reported for	Member mnemonic	Full Legal Entity Name	LEI (if applicable)	Metal Code as per LME terminology i.e. AA, AH, CA, CO, NA, NI, PB, SN, ZS	Type of OTC contract. Can be one of: Averaging Swap Index Physical Other	If Contract Type = 'Other' then field must be populated, otherwise optional description of OTC product	Currency of position	Start date of averaging (if applicable)	End date of averaging (if applicable)	Date of delivery/expiration	Option type 'C' = Call; 'P' = Put Leave blank if not applicable	Strike of option Leave blank if not applicable Round to nearest whole number	Position in metric tonnes. Negative for short position Positive for long position Round to nearest whole number	Equivalent futures position of an option position Leave blank if not applicable Round to nearest whole number
Format	DD/MM/YYYY	CHAR-3	ALPHANUM-256	ALPHANUM-20	CHAR-2	ALPHANUM-9	ALPHANUM-256	CHAR-3	DD/MM/YYYY	DD/MM/YYYY	DD/MM/YYYY	CHAR-1	WHOLE NUMBER	WHOLE NUMBER	WHOLE NUMBER
Sample	11/04/2022	ABC	ABC TRADING LTD	123456789ABCD EFGHIJK	NI	Averaging	Bullet Swap	USD	01/04/2022	30/04/2022	18/05/2022	C	25000	1500	1500