

Energy UK response to Ofgem's Secure and Promote Review consultation

9th February 2018

About Energy UK

Energy UK is the trade association for the GB energy industry with a membership of over 100 suppliers, generators, and stakeholders with a business interest in the production and supply of electricity and gas for domestic and business consumers. Our membership covers over 90% of both UK power generation and the energy supply market for UK homes. We represent the diverse nature of the UK's energy industry – from established FTSE 100 companies right through to new, growing suppliers and generators, which now make up over half of our membership.

Our members turn renewable energy sources as well as nuclear, gas and coal into electricity for over 27 million homes and every business in Britain. Over 730,000 people in every corner of the country rely on the sector for their jobs, with many of our members providing long-term employment as well as quality apprenticeships and training for those starting their careers. The energy industry invests £12bn annually, delivers £88bn in economic activity through its supply chain and interaction with other sectors, and pays £6bn in tax to HMT.

Executive Summary

Energy UK welcomes the opportunity to respond to Ofgem's consultation on changes to the Secure and Promote special licence condition. Energy UK supports any measure which improves liquidity, reduces costs and ensures the market is accessible to all participants. Effective competition in the wholesale market will improve the robustness of prices and lead to lower costs for consumers.

We consider that the main issues Ofgem should consider are:

- **Market structure** – The electricity market is evolving and since the Secure and Promote licence condition came into force in 2014 there has been significant changes to the participants operating in the market with Centrica and Engie selling off significant amounts of generation assets, E.ON separating conventional power generation and global energy trading businesses into Uniper and SSE and Innogy SE agreeing to form a new independent energy supply and services business in GB. This is against a backdrop of increased diversity across the sector and an increase in the number of new market entrants. Ofgem needs to consider how these changes impact liquidity and the Secure and Promote licence condition with any potential changes underpinned by robust and transparent analysis.
- **Long term vision** – We believe that Ofgem should consider a long term vision for how liquidity should be supported going forwards taking account of the significant changes to the power market. This may include looking at what other models are available for creating liquidity as well as how this can move more towards a more natural market spread over a long period of time throughout a trading day. This should also focus on not penalizing any market participant. We suggest that Ofgem set a specific date for this review as soon as possible.
- **Simplification of proposals** - We welcome the introduction of the soft landing proposal and the widening of spreads in fast markets. However, as these changes may increase the complexity of meeting the obligation, Ofgem should consider how the proposals can be made simpler both from an operational and compliance perspective and provide clarity on how it expects MMOs to adhere to the changes.

Energy UK welcomes the opportunity to further discuss the points raised within this consultation as well as wider structural reforms to the Secure and Promote policy with Ofgem. Should you require further information or clarity on the issues outlined in this paper then please contact:

Kyle Martin

Head of Generation Policy
Energy UK
Charles House
5-11 Regent Street
London SW1Y 4LR
Tel: 020 7747 1834
Kyle.martin@energy-uk.org.uk

Response to questions

Question 1: Do you agree with our analysis and proposal for a soft landing?

We agree with Ofgem's analysis that bid-offer spreads move more at the start of a Secure and Promote trading window when price discovery is taking place. This is inherent to the MMO framework with less trades taking place out of the designated windows, hence the price discovery activity generally takes place during the initial period of the windows and prices are therefore more volatile.

We also agree with the proposal to implement a soft landing period of 10 minutes at the start of each window. The bid-offer spread during the soft landing period should be set at 1% to reflect the volatility at the start of the window and allow robust price discovery without leaving MMOs exposed. Whilst we welcome changes that may reduce obligated parties costs of compliance, Ofgem should note, that since this measure will in effect reduce the time that many parties will trade in the market, liquidity and therefore traded volumes, may be impacted.

There is a tradeoff between the time when parties will trade in the Secure and Promote and giving MMOs a soft landing for price discovery. The preference from our members would be for an approach to market making where the market can react to events throughout the day instead of mainly focusing on liquidity into two windows. This would however have to be balanced against potential impact on costs to all market participants

Question 2: Do you have any concerns about the success or unintended consequences of this proposal

We welcome the introduction of the soft landing proposal and changes to the fast market rule. However, these proposed changes may increase the complexity of meeting the obligation, therefore, Ofgem should consider how the proposals can be made simpler from both an operational and compliance perspective and to provide clarity on how it expects MMOs to adhere to the changes. Ofgem should also ensure that the changes do not adversely impact liquidity and should make its analysis available for comment by market participants.

We also suggest that Ofgem actively engage with ICE and Trayport as many market participants will use these trading platforms to meet the Secure and Promote obligation and therefore it will be important that the functionality of these systems are able to facilitate MMOs in complying to the changes in the licence condition and could help design proposals which are easier to comply with.

Question 3: Do you agree with our analysis and proposal to allow bid-offer spreads to widen in response to a fast market?

Energy UK's members have different views on what the trigger point should be and how wide the spreads should widen.

Question 4: Do you have any concerns about the success or unintended consequences of this proposal

Our concerns about the proposal to allow bid-offer spreads to widen in response to a fast market echo those of our response to question 2.

Question 5: Do you agree with the proposed increased spreads

Energy UK's members have different views on what the spreads should be.

Additionally, the limits on the bid-offer spreads may need to be further reviewed as the limits identified as being appropriate prior to March 2014 are unlikely to remain appropriate following implementation of the EBSCR reforms. The cash-out reforms due to be implemented in winter 2018/19 (PAR1 pricing and £6k/MWh VoLL) and therefore we suggest that a review will be required before its implementation.

Question 6: Do you agree with the proposed wording of the modified licence condition

We agree that the proposed wording in the modified license condition accurately reflects the Ofgem proposals.