

**Camilla Eggington
GB Markets
Ofgem
9 Millbank
London
SW1P 3GE**

08th May 2012

Dear Camilla,

Total Gas & Power Ltd (TGP) Response to Ofgem's consultation on Retail Market Review: Intervention to enhance liquidity in the GB power market

Thank you for providing TGP with the opportunity to respond to the consultation on potential intervention measures to enhance liquidity in the GB power market.

TGP is the largest Industrial and Commercial (I&C) gas supplier in the UK and also an electricity supplier supplying 1-2% of the I&C power market. TGP have discussed with Ofgem our serious concerns about the lack of liquidity in the wholesale electricity market, especially in forward markets. Illiquid markets create a barrier to entry and market inefficiencies that risk leaving customers paying more for their supplies than they would if competition were effective.

TGP fully support the 3 wholesale market objectives set out in the consultation and has responded below to each of the questions relating to Mandatory Auction (MA) Ofgem's proposed delivery mechanism. However TGP does not believe that the MA which mandates obligated parties to auction 25% of their generation goes far enough, nor is it the most cost effective solution to deliver liquidity and shape to forward wholesale markets. TGP believes that Ofgem should consider a full self-supply restriction on the large vertically integrated energy companies with appropriate supporting regulation which would provide the liquidity to the market and more effectively underpin competition in the electricity supply market.

A full self-supply restriction would be quicker, easier and less costly for the industry to implement and regulate moving forward. The MA proposals amount to a "partial" self supply restriction, diluted by the fact that the Big 6 energy companies can participate on the buy side and effectively buy back the power that they have put into the auction. As such TGP would ask Ofgem to seriously consider taking the stronger action of a full self supply restriction on large vertically integrated utilities with fully separated generation and supply activities.

However, TGP fully supports Ofgem's attempt to improve liquidity in wholesale markets and as such has answered the specific questions asked in the consultation that relate to Mandatory Auction proposals and provided comments where we believe market features and mechanisms require further development.

TPG believes that Ofgem should set some measurable outputs to judge the success or otherwise of the auctions. It is important that the market sees a signal that Ofgem wants narrower spreads, additional market entry, and improved liquidity. This would also allow Ofgem to review the impacts of the MA and if necessary consider other, or additional, measures.

Should you wish to discuss in any more details please do not hesitate to contact me,

Yours Sincerely



Andrew Green

Head of Regulation
Total Gas & Power
UK Energy Retail



TGP's response to questions in Ofgem's consultation regarding Intervention to enhance liquidity in the GB power market

CHAPTER: One – Objectives for Liquidity

Question 1: Do you agree with the objectives we have identified?

TGP is supportive of the three market objectives outlined in the consultation document but certain aspects of the proposed delivery mechanism would benefit from further development to ensure these objectives are met. TGP also agrees that the focus should be objective 1 (availability of products which support hedging) and objective 2 (Robust reference prices generated along the curve).

Market indications currently suggest that objective 3 (effective near-term markets) is an improving situation, except perhaps for the statement "independents able to meet shaping requirements". TGP suggests, in the response to question 8, that this could be addressed by a robust auction that also delivers shaped products.

TPG believes that Ofgem should set some measurable outputs to judge the success or otherwise of the auctions. It is important that the market sees a signal that Ofgem wants narrower spreads, additional market entry and improved liquidity. This would also allow Ofgem to review the impacts of the MA and if necessary consider other, or additional, measures.

Question 2: Do you think there are other objectives we should be considering?

Yes, all solutions should either compliment or enhance the existing UK forwards market and deliver shaped products to the market. Ofgem policy should always aim to work with the market creating as few distortions as possible.

CHAPTER: Two – Market Developments

Question 3: Do you agree with our views on market developments since summer 2011?

TGP believes that the prompt market shows signs of improved liquidity due to the success of the daily N2EX auction and the actions taken by two of the big 6 suppliers. However, this should have also had a positive effect on the liquidity of the forward curve but this has not been the case, in fact liquidity shown on the curve has actually deteriorated. Poor curve liquidity is in part caused by the lack of clarity within proposals under Electricity Market Reform (EMR) such as the uncertainty surrounding the new carbon floor price as well as CFD FIT and cap mechanisms.

While TPG agrees with Ofgem that there have been recent improvements, developments have yet to secure a transparent, liquid market which is required.

Question 4: What specific further developments would be necessary to meet our objectives?

TGP believes a full self supply restriction on large vertically integrated utilities with fully separated Generation and Supply activities would be the best way for Ofgem to meet its objectives with respect of liquidity in wholesale power markets.

TPG believes that Ofgem can create a licence condition that requires the Big 6 to sell 100% of their generation output to third (unrelated) parties. There should be a specification that the Big 6 prove that a proportion of those sales. The remainder of their obligation can be evidenced via contract notification to third parties under the BSC systems. The obligation should also specify that the terms must be reasonable, allowing parties who cannot secure reasonable terms to come to Ofgem and report any such licence breaches.

The benefit of this regime over an MA is that it would allow parties to come to market with the products that meet the needs of buyers. It is probable that volume will appear in auctions, but it will also allow bigger parties to take larger positions and then divide products into value added propositions for smaller suppliers and new market entrants.

Question 5: Do you agree that objectives one and two are current priorities given market developments?

Yes the situation has improved with respect to objective 3 but the market would improve further if hourly shape is made available to be bought in longer term auctions.

CHAPTER: Three – Ofgem’s proposal for a mandatory Auction

Question 6: Do you agree that the MA is the appropriate mechanism to meet our immediate objectives?

No, TPG believes that a self-supply restriction could deliver greater liquidity faster than the MA.

However, if Ofgem still feels the MA could deliver against their objectives, TGP is would support the MA proposals with the suggested modifications set out in question 8 which are critical to ensuring that Ofgem delivers its objectives and market features that will underpin effective competition.

Question 7: Do you agree that, at the present time, the other mechanisms identified would not be appropriate for Ofgem to pursue?

No. TPG would like to see the self-supply restriction revisited. This could be a requirement that all of their volume moves via an auction, but the 25% proposed does not look sufficient to deliver real liquidity.

CHAPTER: Four – Proposed detailed design features

Question 8: Do you agree with the key features of the MA we set out?

TPG would ask Ofgem to consider the following with respect to the design of the Mandatory Auction.

- A range of products to encourage participation of small suppliers but most critically a mandatory auction on an hourly price basis with a small clip size would allow suppliers to shape their requirements. Products sold should allow the buyer of such products to lift them at delivery on an hour by hour basis to allow for shape matching of demand. (i.e. not just flat base-load and peak products).

- The range of products should be developed, specified and consulted upon in co-operation with small suppliers to check that they deliver what small suppliers would want to buy.
- There should be a continuous auction with minimum daily / weekly volumes and not a periodic monthly auction with participation window which may be vulnerable to price spikes and would not provide the flexibility that the market requires.
- A zero reference price would allow for true price discovery. It may cause abnormally low prices initially but the impact is likely to be more financial players taking an interest in the UK market again which should eventually create a more robust reference price.
- Forward shaped products should be sold in a staged depletion manner with newer periods with large volumes and a gradual reduction further along the curve rather than made available in large blocks or all in one period.
- Obligated parties should be subject to strict buy-side rules with a net sell obligation (rather than being able to buy more than they have sold). If obligated parties needed to buy back volumes sold in the auction then they should use the forward market to do this. The buyers of volumes bought in the auction will be hedging this larger expense in the forwards market improving the liquidity along the curve.

Question 9: Do you consider it appropriate to have buy-side rules in place and do you have any comments on the detail of such rules?

Yes, TGP would support robust buy-side rules – see response to question 8 regarding net sell obligation.

CHAPTER: Five – Identifying a Platform

Question 10: Do you consider that there are benefits and risks to the approaches that we have not identified?

Multiple platforms would have an adverse affect on industry credit and collateral arrangements which may prevent smaller suppliers from participating which would be detrimental to Ofgem's objectives.

Question 11: Which approach do you consider is best placed to deliver our objectives at least in terms of cost and risk?

TGP would strongly support Approach 1 with one single platform and clearing house provided by an Ofgem administered procurement process. Obligated parties should not be able to make their own arrangements – this would make it more complex, less transparent, more difficult to regulate and add to small suppliers' credit and collateral burden

Question 12: Do you consider that both approaches are able to meet our objectives?

No, only approach one.

