



E.ON's response to Ofgem's November 2013

Wholesale power market liquidity: statutory consultation on the 'Secure and Promote' licence condition and supporting documentation

Executive Summary

E.ON supports the development of sustainable competition in all parts of the electricity and gas supply chains for the benefit of customers. This includes greater levels of liquidity in the electricity wholesale market. Indeed our own business model is based on the availability of liquid markets. As a net purchaser of wholesale power and gas we want to see sustainable competitive markets where there is a continual improvement in the ability to trade. This means we support Ofgem's aims behind its wholesale power market liquidity work, but are not sure that the proposed execution, in the form of the proposed special generation licence condition "Liquidity in the Wholesale Electricity Market" is the right approach, or that the current drafting makes it a licence condition companies can accept.

We believe that to support additional trading and help build customers' trust, all licensed generators and suppliers (electricity and gas) need to be subject to:

1. separate organisational management (business separation) of any licensed generation and supply (electricity and gas) activities within a corporate group;
2. a prohibition on cross-subsidy between any generation and supply (electricity and gas) activities within a corporate group; and
3. a prohibition on discrimination in the buying and selling of electricity and gas.

We are concerned that Ofgem's impact assessment appears to be measuring the predicted benefits of introducing the proposed licence condition against a model that is not representative of the Great Britain wholesale power market in 2013. Ofgem is presenting the generation licensees as if they were each a vertically integrated corporate group not operating in a market. To be using such a model for the impact assessment means that Ofgem will be making its decision based partly on an error of fact.

The overall principles of the proposed licence condition, as currently drafted, raise concerns that generation licensees, by virtue of being in the wrong corporate group, are being required provide services that do not form part of a generation business. Each licensee is being required to subsidise these services to an extent that the total size of the subsidy can, for some, be greater than the licensee's turnover, with the consequential risk of the licensee not being able to finance these activities.

We also disagree with Ofgem's rationale as to why it has selected the generation licensees of eight corporate groups (the "Relevant Licensees"). We believe that the rationale is sufficiently flawed as to suggest that Ofgem's decision is an arbitrary discrimination against these eight organisations.



The Supplier Market Access service, within the proposed licence condition, is similar to the provision of a volume aggregation service, which E.ON has recommended over the last few years. However, Ofgem's proposal appears more costly, compared to a single volume aggregation service, and discriminatory against those providing the service.

The Market Maker obligation, within the proposed licence condition, is introducing a non-commercial price regulated market making service. Such an arrangement is unlikely deliver the effect Ofgem has set for justifying this intervention, namely creating robust prices along the curve that can be used in supporting the settlement of CFDs.

The current drafting of the proposed licence condition and the three schedules within it, raise a set of concerns that broadly fit into the following five categories;

1. The relationship between Relevant Licensees and their affiliates, which this concern would be resolved if there was clarity that affiliated Relevant Licensees could act together to achieve compliance;
2. The cost of providing the services and the cost of risk, which this concern would be resolved if the licence condition was amended to allow full recovery of costs and risk premiums;
3. The impractical nature of the obligations, which this concern would be resolved if there was a clear recognition that these activities are outside normal generation business activities and by amending the absolute requirements of the proposed licence condition to instead require the use of reasonable steps to secure delivery of the requirements;
4. The criteria for a licensee being captured under this licence condition, which this concern would be resolved if the proposed licence condition was amended to be a standard licence condition that had clear and fixed criteria as to when a licensee becomes subject to these compliance obligations; and
5. MiFID II and EMIR regulations, where to resolve this concern a guarantee is needed within the licence condition that if market making in wholesale power places the Relevant Licensee under these two regulations and the Relevant Licensee had, using reasonable steps, been unable to secure the services of a Nominee, then the requirement to provide the Market Making service would be suspended.

We are also seeking a development period between the decision to implement the proposed licence condition and it becoming effective. This is to give time for the Relevant Licensees to setup the provision of the two services.

Unless these concerns can be resolved, it is difficult to see how the generation licensees that will be subject to the requirements of the proposed licence condition can accept such unreasonable costs, obligations and risks.



E.ON's response to Ofgem's November 2013

Wholesale power market liquidity: statutory consultation on the 'Secure and Promote' licence condition and supporting documentation

1. Introduction

This response is on behalf of the E.ON SE Group and in particular E.ON's generation licensees, Citigen (London) Limited, E.ON UK plc, E.ON Climate & Renewables UK Humber Wind Limited, E.ON Climate & Renewables UK Rampion Offshore Wind Limited and Enfield Energy Centre Limited. The Authority has served notice that it proposes to modify the electricity generation licences held by these five licensees by introducing a new proposed special condition "Liquidity in the Wholesale Electricity Market", which Ofgem also refers to as "Secure and Promote" and "S&P". Under the proposal these five generation licensees will be "Relevant Licensees".

E.ON supports the development of sustainable competition in all parts of the electricity and gas supply chains for the benefit of customers. This includes greater levels of liquidity in the electricity wholesale market. Indeed our own business model is based on liquid markets. As a net purchaser of wholesale power and gas we want sustainable competitive markets where there is a continual improvement in the ability to trade. This means we support Ofgem's aims behind its wholesale power market liquidity work, but are not sure that the proposed execution, in the form of the proposed special generation licence condition is the right approach, or that the current drafting makes it a licence condition companies can accept.

In Chapter 2 we consider ways of supporting additional trading and helping to build customers' trust. We consider how a new licence condition could contribute to this. We also make proposals to support additional trading and help build customers' trust.

In Chapter 3 we discuss Ofgem's "Wholesale power market liquidity: statutory consultation on the 'Secure and Promote' licence condition impact assessment". Through answering the questions it sets, we explain our concerns with Ofgem's analysis.

In Chapter 4 we present an overview of Ofgem's Liquidity in the Wholesale Electricity Market licence condition proposals. This is accompanied by Chapter 5, which provides comments on the detail of the proposed licence condition and its three schedules.

Ofgem has issued its draft "Liquidity in the Wholesale Electricity Market (Special Condition AA of the electricity generation licence): Guidance" (the "Draft Guidance"). Our suggestions for amendments to the Draft Guidance are covered in Chapters 4 and 5. The final form of the Guidance is dependant on feedback, such as this, and any further amendments to the actual licence condition and its three schedules. We ask that Ofgem discusses any changes to the Guidance and the licence condition with all of the potential Relevant Licensees before the final decision is published.



2. Supporting additional trading

Ofgem's proposals for supporting additional trading

We understand that Ofgem's aims from introducing the proposed licence condition are now:

1. Providing support for small suppliers, through introducing a Supplier Market Access service; and
2. Securing robust reference prices along the curve, through increased trading along the curve, by introducing a price regulated Market Making service.

The two services are to be supported by a reporting requirement.

Supplier Market Access service

The proposed Supplier Market Access service, which is Schedule A within the proposed licence condition, is similar to the provision of a volume aggregation service, which E.ON has been recommending over the last few years. However, Ofgem's proposal appears not to provide as an efficient solution, or provide such a broad service, as a single volume aggregation service could.

As proposed, the Supplier Market Access service does not provide the support to small independent generators, or the level of support to small suppliers, that a volume aggregation services would have provided. Because small generators with their provision of small volumes of power are excluded, the costs of operating the Supplier Market Access service are likely to be greater than if they had been included.

Ofgem's impact assessment presents estimated costs of up to £1m per year per provider for providing the Supplier Market Access service¹. The proposed licence condition requires the Relevant Licensees to base their prices for this service on wholesale market prices. Consequently the Relevant Licensees will be offering products at very similar prices. With regulated uniformity of prices, we fail to see any benefits for customers from the industry having to absorb the cost of having eight companies spending up to £1m per year each to offer the same wholesale market prices. Given the required uniformity of prices it would seem that having just one provider would deliver the least cost solution.

The current drafting of the Supplier Market Access rules raises number of significant concerns as to how the Supplier Market Access service can be implemented and operate in a fair and non-discriminatory way. Unless these concerns are fully resolved it is

¹ Ofgem's Wholesale power market liquidity: statutory consultation on the 'Secure and Promote' licence condition - Impact Assessment Figure 2 page 29 (Low case £178,000, Best estimate £457,000, High case £1,063,000).



difficult to see how the licensees that are to be subject to providing the Supplier Market Access service can accept the proposed licence condition.

Market Making obligation

We understand the ideas behind introducing a market maker obligation, in that it could support more robust prices of certain wholesale market products along the forward curve. However, we do not believe a non-commercial price regulated market making service will deliver robust prices along the forward curve. Such derived prices will not be sufficiently robust to reliably support the settlement of CFDs. An example of why this could happen is that the Relevant Licensees, or their Nominees, while having to post bids and offers, will not be required to have corresponding trading agreements with counterparties. This means that phantom bids and offers could form the bulk of the bids and offers used to set reference prices. Consequently, the proposed arrangement is unlikely deliver the effect Ofgem has set for justifying this intervention. The settlement of CFDs needs to be against the actual trades that are carried out at the most liquid point on the curve. That means, for power in Great Britain, settlement being against the day-ahead auction prices.

The current drafting of the proposed Market Making rules raises a number of concerns as to how the obligations for the proposed Market Making service could be implemented and operate in a fair and non-discriminatory way. Unless these concerns are fully resolved it is difficult to see how the licensees that are to be subject to providing the Market Making service can accept the proposed licence condition.

Secure and Promote reporting requirements

Increased levels of reporting will support greater transparency and fairer competition between all generators and all suppliers. Ofgem's proposals for Secure and Promote (Liquidity in the Wholesale Electricity Market) reporting are therefore welcome. However, we believe the proposals do not go far enough, particularly in the reporting of "Additional Information".

The reporting of Additional Information should cover all corporate groups with generation and supply licensees. A monthly report to Ofgem should cover monthly totals of their total licensed generation volume (disregarding generation for onsite consumption and imports), licensed electricity supply volume and all power trading volume that was for delivery in that month. The current proposals only cover volumes from trading with Eligible Suppliers, market making and day-ahead auctions. To aid transparency this information, other than any forward looking information, should then be published by Ofgem.



E.ON's proposals for supporting additional trading

In 2012 E.ON's Great Britain generation and supply licensees generated 27.4TWh and supplied 49.4TWh² of electricity respectively, meaning the licensed electricity supply activities supplied 80% more electricity than the licensed generation activities generated. Even after allowing for licence exempt generation and supply, this made E.ON a large net purchaser of electricity and gas. As a net purchaser of electricity and gas, we want to see greater volumes of electricity and gas being made available for trading between unrelated parties. This would provide greater transparency, fairer competition between all generators and also between all suppliers (electricity and gas) and secure larger potential volumes for hedging by all generators and suppliers (electricity and gas). However, Ofgem's proposed licence condition currently presents too many issues for it to deliver this. To achieve the greater levels of trading, and help build customers' trust, there needs to be:

1. no cross-subsidy between generation and supply (electricity and gas) within vertically integrated companies; and
2. no discrimination in the buying and selling of electricity or gas.

This means all licensed generators and suppliers (electricity and gas) being subject to:

1. separate organisational management (business separation) of any licensed generation and supply activities within a corporate group;
2. a prohibition on cross-subsidy between any generation and supply activities within a corporate group; and
3. a prohibition on discrimination in the buying and selling of electricity and gas.

These three requirements should be implemented regardless of if the proposed licence condition is introduced or not. Their presence would support competition directly and enhance the otherwise limited competitive effects of the two services provided by the proposed licence condition.

Separate organisational management (business separation) of any generation and supply activities within the licensee's group

Customers and the general markets must be able to trust that the electricity and gas markets are operating efficiently. The cost of any economic inefficiency, through conflicts of interest associated with licensed generation and licensed supply (electricity and gas) activities being managed as a single business unit, needs to be avoided. Also, there needs to be confidence that Ofgem has the power to investigate and take appropriate action if such situations are found.

² E.ON's UK Consolidated Segmental Report for the year ended 31 December 2012



E.ON has separate organisational management of its licensed generation (E.ON Climate & Renewables and E.ON Global Generation) and licensed supply (E.ON Regional Unit UK, for the UK) businesses. Because CHP generation is often dependent upon the customer's heat demand, in the UK, management of E.ON's CHP activities is within the supply business. The generation business does not trade power directly with the supply business. E.ON Global Commodities, which manages all of E.ON's European trading operations, has activities that include purchasing generation from the generation business and providing electricity and gas to the supply business. These arrangements are covered by cross border contracts, which are prepared on an arm's length basis (meaning that although the transactions are between two related or affiliated parties, they are conducted as if the two parties were unrelated) and are subject to examination by the tax authorities in Germany and the UK.

For a number of reasons we believe that there is a need for separate organisational management (business separation) of licensed generation and licensed supply (electricity and gas) within all vertically integrated groups that have licensed generation and licensed supply (electricity and gas). Our primary reason for this is to promote greater trading and thus confidence in the trading, but also to provide more reassurance on the whole area of transfer pricing. To achieve this, we believe that there should be separate organisational management (business separation) for vertically integrated groups, with their licensed generation activities and the licensed supply (electricity and gas) activities ring fenced from each other, such that an individual company could not be a generation licensee and a supply (electricity or gas) licensee. Also, as a minimum, there should also be:

1. a requirement for separate management of the licensed generation business and the licensed supply (electricity and gas) business;
2. a prohibition on the direct electricity and gas trading between related generation and supply (electricity and gas) licensees; and
3. a requirement that all internal procurement from related third parties of electricity and gas by supply licensees be matched by identical external trades on the wholesale market, plus a transparent agent's fee, which was reflective of market price.

During the debates on liquidity, leading to the proposed Liquidity in the Wholesale Electricity Market licence condition, it has been suggested that corporate groups, such as E.ON, were not trading large volumes in the power market. While we believe E.ON was, and still is, trading large volumes, we have sought to support customer trust and secure that others were trading large volumes also. We therefore called for a generation and supply (electricity and gas) licence requirement that all licensees trade minimum volumes of electricity and gas with unrelated parties. With separate organisational management (business separation) all electricity and gas procurement by licensed suppliers would be wholesale products at wholesale price, plus a transparent agent's fee. This would not only increase the volume of energy brought to the market for trading, but it would also ensure all product shapes were available for trading. This would remove the need for a licence condition forcing the trading of minimum volumes, of electricity



and gas with unrelated parties. Obviously, if Ofgem should not wish to introduce separate organisational management (business separation), then the introduction of generation and supply (electricity and gas) licence requirements, for all licensees, for the trading of minimum volumes of electricity and gas with unrelated parties would still be needed to support customer trust.

Separate organisational management (business separation) as a licence condition would also mean that Ofgem would have the powers to investigate and take appropriate action if such managerial separation of licensed generation and licensed supply (electricity and gas) was found not to be operating within a vertically integrated organisation. This would provide additional confidence that the licensed supply (electricity and gas) by vertically integrated groups was independent of any generation by generation licensees within the supply licensee's corporate group.

A prohibition on cross-subsidy between any generation and supply activities within the licensee's group

Cross-subsidy between generation and supply businesses of vertically integrated companies could lead to economic inefficiency in the wholesale market. E.ON's own transfer pricing arrangements are designed to prevent cross-subsidy between its generation and supply activities. However, customers' trust and the general market's trust would increase if it was widely understood that cross-subsidy between generation and supply activities was prohibited and that if it was suspected Ofgem could investigate and take appropriate action.

To provide trust that cross-subsidy is prohibited, the amending and switching on of the Generation Licence Condition 17A, *Prohibition of Cross-Subsidies*, and the Electricity Supply and Gas Supply Licence Conditions 19B, *Prohibition of Cross-Subsidies*, for all licensees is required. This would provide a clear and consistent prohibition of cross-subsidy between the licensed generation and licensed supply (electricity and gas) activities.

A prohibition on discrimination in the buying and selling of electricity and gas

Customers and the general market must be able to trust that there is no barrier to trading being created through discrimination in trading of electricity and gas. E.ON is already prohibited from such discrimination in electricity under the existing Generation Licence Condition 17, *Prohibition of Discrimination in Selling Electricity*. If there was suspicion that E.ON was discriminating in the selling of electricity, Ofgem would be able to investigate and take appropriate action.

Licence Condition 17 does not deliver the required level of trust it could. This is because it is active only for a very limited number of licensees. To secure that all licensed generators are offering fair and reasonable terms when negotiating trading agreements, Licence Condition 17 should become active for all generation licensees. If it is believed that it is not appropriate to have Licence Condition 17 active for all generation licensees,



then the question has to be asked why does it remain active for E.ON UK plc, when that company has a relatively small market share?

To support small generators in particular, the principles of the existing Generation Licence Condition 17 should also be incorporated in all electricity and gas supply licences, in the form of a prohibition of discrimination in purchasing electricity and gas. Here the licence condition should set out that the licensee and its affiliates must not purchase or offer to purchase electricity or gas from any one provider or person seeking to become a provider on terms as to price that were materially more or less favourable than those on which it purchases or offers to purchase electricity or gas from comparable wholesale providers.



3. Ofgem's Impact Assessment

We are concerned that Ofgem's impact assessment appears to be measured against a model that is not representative of the Great Britain wholesale power market in 2013. Ofgem is presenting the generation licensees as if they were each a vertically integrated corporate group not operating in a market. For E.ON that is not the situation, which suggests that to be using such a model for the impact assessment, Ofgem will be making its decision based partly on an error of fact.

Four of E.ON's five Relevant Licensees are not supply licensees and the other, E.ON UK plc, is only a non-domestic supplier. For the avoidance of doubt, none of E.ON's Relevant Licensees are domestic suppliers. However, Ofgem stated in its June 2013 document that "*the parties subject to the market making obligation have a substantial presence in both generation and domestic supply markets. Vertical integration provides an alternative to wholesale market trading that is not available to independent players. While the proposed licensees do participate in the wholesale market, they have a continuous option to source energy from their affiliate business as an alternative*"³. That is clearly incorrect for the E.ON parties.

It may be that in its June 2013 document, Ofgem intended to say "*the corporate groups of the parties subject to the market making obligation have a substantial presence in both generation and domestic supply markets. Vertical integration provides an alternative to wholesale market trading that is not available to independent players. While these corporate groups do participate in the wholesale market, their supply businesses have a continuous option to source energy from their generation business as an alternative*". However, E.ON UK plc is subject to the Generation Licence Condition 17A, *Prohibition of Cross-Subsidies*, and the Generation Licence Condition 17, *Prohibition of Discrimination in Selling Electricity*, meaning that it cannot provide preferential arrangements for E.ON's supply business and, as described above, both the generation and supply businesses are trading solely at wholesale market prices. Therefore, even if Ofgem meant corporate groups, when it referred to parties and licensees, the statement would still be incorrect for E.ON.

In its impact assessment Ofgem states that "*As firms compete, they will look for ways to make their prices more competitive, exerting downward pressure on the prices paid by consumers. These may include reducing their profit margins, or reducing their operational costs.*"⁴ This suggests that at the moment Ofgem believes the licensees do not compete, which suggests that Ofgem's reference model is based on a monopoly structure. Using a monopoly structure as a reference model is clearly wrong. We discuss this in more detail in our answer to Ofgem's Question 5, below.

³ Wholesale power market liquidity: final proposals for a 'Secure and Promote' licence condition June 2013 paragraph 2.8

⁴ Ofgem's Wholesale power market liquidity: statutory consultation on the 'Secure and Promote' licence condition - Impact Assessment paragraph 5.17.



Ofgem's Impact Assessment Questions

Question 1: *Do you agree with our description of the key issues and objectives for our Secure and Promote proposals?*

While we would not agree with some of the conclusions drawn by Ofgem, we generally agree with Ofgem's description of the key issues and objectives for Ofgem's Secure and Promote (Liquidity in the Wholesale Electricity Market) proposals.

Question 2: *Do you agree with our evaluation of the impact of our Secure and Promote proposals on consumers?*

We generally agree with Ofgem's evaluation of the impact of the Secure and Promote (Liquidity in the Wholesale Electricity Market) proposals on consumers. We also agree that it is difficult to provide a quantitative estimate of the potential impact on consumers' bills from greater liquidity. Consequently, the risk is that Ofgem's assumptions are wrong and the industry incurs net costs, which in the long-term would inevitably have to be met by customers.

We agree with Ofgem that the introduction of the proposed licence condition will create some costs for the proposed Relevant Licensees, which at the moment, we believe, look discriminatory. However, we disagree that the costs can be passed on, given our belief that the wholesale market is already competitive. For generators operating in a competitive market the only costs they can pass to the market are those that are common to all. In such a situation costs incurred by generators for providing services that are unrelated to generation and not common to all generators cannot be passed on to the market. Ofgem needs to explain how the companies can fully recover their costs and how it is not creating a situation where certain licensees are discriminated against and forced to subsidise their competitors. Without fair protection the Relevant Licensees cannot be expected to accept such proposals.

Question 3: *Do you agree with our evaluation of the impact of our Secure and Promote proposals on competition?*

We support Ofgem's objective, which is the facilitation of greater competition for the benefit of customers, if the greater competition was sustainable. We would therefore support the proposed Supplier Market Access service, if all the costs of providing such a service were covered by the whole industry. However, not to fairly share those costs is to discriminate against the Relevant Licensees and so create a new market distortion and the consequential adverse risk to competition.

As Ofgem explains, it is "only proposing to place the S&P licence condition on certain firms. S&P licensees will incur costs which their competitors will avoid. This could affect



*the relative competitiveness of firms with and without the S&P licence condition*⁵. We would add that generators are competing in a competitive market; in such a market, while the cost of such a licence condition is relatively small, it is not likely to have an insignificant impact on the Relevant Licensees' competitiveness. The proposed licence condition is introducing a new market distortion and the consequential adverse risk to competition.

In relation to the Market Making services specifically, the Relevant Licensees will incur costs that may be partially offset by the benefits from increased liquidity. However, this benefit is likely to be outweighed by the cost of having to subsidise their competitors and the consequential negative impact on competition.

Question 4: *Do you agree with our evaluation of the impact of our Secure and Promote proposals on sustainable development?*

We broadly agree with Ofgem's evaluation of the impact of its Secure and Promote (Liquidity in the Wholesale Electricity Market) licence condition proposals on sustainable development. Notwithstanding our view that day-ahead auction prices should be used for the settlement of CFDs, we note that the market making obligation is presented as helping the market to provide a CfD reference price, in particular a baseload CfD reference price. As the Relevant Licensees are being required to subsidise market making, they are in effect being used to subsidise the settlement of baseload CfDs.

Question 5: *Do you agree with our evaluation of the cost impacts of our Secure and Promote proposals?*

If Ofgem's intention is that the E.ON SE Group will provide one version of each service, then we believe Ofgem's estimate of the cost impacts are broadly in line with ours. However, if the intention is as per the current drafting of the licence proposal, then the costs are significantly higher than Ofgem's estimates. This is because E.ON's five Relevant Licensees do not have trading functions and therefore they would each have the cost of establishing and then operating such trading functions.

We question Ofgem's comparing of costs to benefits. As noted above, Ofgem portrays a generation market where at present generators do not compete and then goes on to estimate the benefits of introducing competition. The generation market is already competitive; generators are competing with each other. Any assessment has to be by how much can the level of competition be raised, what can support such an increase and, for such an incremental increase, what are the benefits. Competition has already delivered reduced profit margins and reduced internal operational costs. Greater levels

⁵ Ofgem's Wholesale power market liquidity: statutory consultation on the 'Secure and Promote' licence condition - Impact Assessment paragraph 3.19.



of competition will now come mainly from innovation, such as the introduction of new technology, which result in reduced operating costs and better customer service. However, improved competition through innovation only produces the incremental benefit, not the full benefit of introducing competition as Ofgem seems to be suggesting. Therefore, the benefits from an incremental increase in competition are unlikely to deliver the financial benefits to customers that Ofgem is suggesting.

Of concern is Ofgem's suggestion that the Relevant Licensees may have to reduce their profit margins, if they were to start competing with each other. Notwithstanding that generators are already competing with each other, the implication is that Ofgem believes that generators should reduce their profits further. Ofgem's analysis shows *"that the break-even reduction in operational costs needed to deliver benefits equal to the ongoing costs of S&P would be 0.5%. For profits, the respective reduction is 0.8%. A combination of smaller reductions in both operational costs and profits could also deliver sufficient benefits to cover the ongoing costs. The break-even changes required are therefore very small in relation to the overall size of operational costs and profits."*⁶ Clearly Ofgem's proposals are introducing profit cap regulation, by introducing a 0.8% reduction in average EBIT of Relevant Licensees. This is at a time when it is widely recognised that conventional generators' profits are under pressure.

By requiring generators to reduce profits to subsidise market interventions, generators are being made less profitable at a time when they are being encouraged to invest in new plant. Having to incur subsidy costs will make investment in new plant less attractive and so place an increased risk on security of supply.

Question 6: *Do you agree with our evaluation of the risks and unintended consequences of our Secure and Promote proposals?*

We do not agree with Ofgem's evaluation of the risks and unintended consequences of its Secure and Promote (Liquidity in the Wholesale Electricity Market) proposals. Below, we comment on a number of the areas Ofgem has considered.

Market making having limited effect on volumes

We disagree with Ofgem that for both of the proposed services the costs incurred are largely proportional to the volume traded. Both services are new and will have significant fixed costs, which have to be covered, regardless of the level that the service is used, or the size of the Relevant Licensee's generation business. Sustainable benefits to the market and therefore customers will only materialise if there is a large usage of the services. Therefore, the cost impact will not be proportional to the benefits, or be the same for all licensees. We fear that for the smaller Relevant Licensees the costs of

⁶ Ofgem's Wholesale power market liquidity: statutory consultation on the 'Secure and Promote' licence condition - Impact Assessment paragraph 5.19.



providing these services will be relatively so great that these Relevant Licensees will not be able to finance these activities.

Intervention may crowd out commercial activities

Ofgem is correct that the imposed market making arrangements might reduce the potential for commercial market making agreements. However, Ofgem is not correct to assume that commercial market makers could seek to provide an improved service, through narrower spreads or greater availability. The introduction of price regulation of market making, at a below cost price, restricts market making to just those who are being forced to act in a non-commercial manner, under obligation, to provide and subsidise the Market Making service.

Risk of decreasing liquidity outside trading windows

Ofgem is correct that increasing activity in trading windows will make them more attractive for trading, given the fact that the cost of the Market Making service is to be subsidised. This will create a risk that existing activity in other periods will move into the windows. While some companies will still look to trade at other times based on their needs, the risk is that pure traders will focus just on the windows. There is a significant risk that the wholesale power market will become illiquid outside of the window periods.

There is also the risk that liquidity will be focused on the products that are supported by the subsidised Market Making service. As a consequence, suppliers may find it harder to secure products that are not covered by the subsidised Market Making service.

Perception of greater regulatory risk

Introducing the Liquidity in the Wholesale Electricity Market licence condition expands the scope of regulation in the Great Britain power market. This along with the other interventions that Ofgem has taken has damaged perception of investors about the regulatory stability of the market. This particular intervention suggests that Ofgem is now prepared to direct generators to undertake activities that do not form part of generation, is prepared to introduce price regulation of those new activities and cap the profits of generation licensees. Regardless if Ofgem is convinced that intervention in this case is now warranted, those considering new generation projects have to factor in significant regulatory risk. That increases the risk that some projects will not now go forward creating a negative impact on long-term security of supply.

The apparent objective of having eight corporate groups providing the same regulated service is clearly not the most economically efficient way of supporting small suppliers. By not striving for the most economic solution Ofgem is signalling that it is prepared to introduced unnecessary costs to the wholesale market. Such actions support the perception of greater regulatory risk.



Compliance risk for S&P licensees

As Ofgem has recognised, the introduction of a new licence condition would create compliance risks for the Relevant Licensees. Ofgem states that "*Failure to meet the requirements will lead to them being in breach of their licences and potentially liable for financial penalties*".⁷ However, the proposed licence condition's drafting requires absolute compliance for positive delivery of operational objectives, which means that accidental breaches of the licence condition will be inevitable.

The imposition of an absolute requirement to carry out positive operational actions, such as making bids and offers available, is unreasonable. Unless the licence condition is modified so as to reflect the reality that carrying out positive operational actions has to be based on taking reasonable steps to secure delivery of compliance, then the compliance risk of the proposed licence condition will be unacceptable.

We discuss this issue in greater detail below, within the "Impractical nature of the obligations", in Chapter 4.

Uncertainty over European financial legislation

Ofgem recognises changes to European financial legislation are unlikely be completed by the time of a decision on whether to introduce the Liquidity in the Wholesale Electricity Market licence condition. In recognition of this, it has helpfully introduced the use of Nominees. However, the current drafting creates an absolute requirement to carry out market making. Compliance is required even in a situation where it is not practical for the Relevant Licensee's corporate group to carry out market making and it has tried to secure the services of a Nominee, but has found the cost unreasonable. This is discussed further in Chapter 4's discussion on MiFID II and EMIR.

⁷ Wholesale power market liquidity: statutory consultation on the 'Secure and Promote' licence condition – Impact Assessment paragraph 6.11



4. Overview of Ofgem's Liquidity in the Wholesale Electricity Market licence condition proposals

The overall principles of the Liquidity in the Wholesale Electricity Market licence condition raise seven points of concern, namely that generation licensees, by virtue of being in the wrong corporate group, are being:

1. Required to provide Market Access services and Market Making services; both activities that do not form part of a generation business;
2. Required to subsidise the activities of providing Market Access services and Market Making services;
3. Required, through the provision of the two services, to provide subsidies, the total size of which can be greater than the licensee's turnover, with the consequential risk of the licensee not being able to finance these activities;
4. Required to provide subsidies to others, by operating as if they were a monopoly licensee that could pass on such costs to customers, while actually operating in competitive markets where such costs cannot be passed on;
5. Required to impose Ofgem's price regulation of market making in the wholesale power market;
6. Subject to regulated profit caps; and
7. Required to deliver a subsidy introduced by a government body (Ofgem), which could therefore be classed as State Aid, in a form that is not transparent and is discriminatory in the allocation of costs.

As explained above, we also disagree with Ofgem's rationale as to why it has selected eight corporate groups. We believe that the rationale is sufficiently flawed as to suggest that Ofgem's decision is an arbitrary discrimination against these eight organisations.

These concerns and the poor drafting of the proposed licence condition lead us to believe that the draft licence text, including the three schedules, does not reflect Ofgem's final policy position.

In addition to the seven points above, as currently drafted the proposed licence condition and its three schedules also raise a number of further concerns. These broadly fit into the following five categories;

1. The relationship between Relevant Licensees and their affiliates;
2. The cost of providing the services and the cost of risk;
3. The impracticable nature of the obligations;
4. The criteria for a licensee being captured under this licence condition; and
5. MiFID II and EMIR.



The relationship between Relevant Licensees and their affiliates

Within the E.ON SE Group there are five generation licensees. It appears that for each of them the proposed licence condition will apply, all five will be Relevant Licensees. As currently drafted the proposed licence condition refers only to the licensee, which suggests that E.ON has to provide five versions of each service. Also, the proposed licence condition's Schedule B paragraph 4 sets out that "*the licensee may not nominate a person as Nominee in relation to a month if that person is also nominated as Nominee [in relation to that month by two other Relevant Licensees]*". This suggests that E.ON's Relevant Licensees will not be able to all use the same Nominee and thus they cannot operate as a single unit, or collectively secure the services of a single Nominee.

Requiring five companies from the same corporate group to each provide the two services will impose costs on the industry and, in the long-term, customers. These costs will be five times greater than necessary, with no increase in competition. Five companies from the same corporate group should not be competing against each other. The Guidance helpfully states that "*Our 'Secure and Promote' (S&P) policy is being introduced through a special condition, inserted into all generation licences held by certain company groups. (For the avoidance of doubt, the obligation only needs to be met once by each group).*"⁸ There is clearly a misalignment between the current drafting of the licence condition and the Guidance.

We ask that clear consistency is introduced between the licence and the Guidance so that it is clear that:

1. a corporate group only has to provide one version of each service;
2. Relevant Licensees within a corporate group can combine their obligations so that they can deliver just one version of each service for the corporate group, including procuring the services of a Nominee; and
3. Relevant Licensees within a corporate group can individually, or collectively, subcontract the delivery of the licence obligations to a third party, where the third party can be an Affiliate of the licensees (including Affiliates that are Relevant Licensees) or an unrelated third party (including unrelated Relevant Licensees).

For Affiliate we are referring to the generation licence definition of; "*in relation to any person means any holding company of such person, any subsidiary of such person or any subsidiary of a holding company of such person, in each case within the meaning of sections 1159 and 1160 of the Companies Act 2006*".

⁸ Liquidity: in the Wholesale Electricity Market (Special Condition AA of the electricity generation licence):Draft Guidance paragraph 1.3



The cost of providing the services and the cost of risk

The licence condition should apply to all licensed generators and suppliers who routinely enter into contracts with unrelated companies for the buying and selling of power, or whose affiliates and related undertakings or other third party agents do on their behalf. We therefore disagree that Ofgem's proposed Schedule A and Schedule C should only apply to eight companies.

We also disagree that that Ofgem's proposed Schedule B should only apply to generation licensees that are from six corporate groups, mainly because:

1. we disagree that a generation licence should be used to make the facilitation of market making a requirement to be able to operate generation plant;
2. we do not believe Ofgem has provided sufficiently robust evidence as to why other activities within certain generation licensees' corporate groups, make those corporate groups appropriate for being compelled to providing the Market Making service; and
3. regulated market making is a service to help all generators and suppliers, although it will obviously help speculators as well, therefore its facilitation and cost should be shared by all generators and suppliers; to just single out six corporate groups' generation licensees would be discriminatory.

Ofgem has set out three areas where six organisations are present, namely; the domestic supply market, vertical integration and trading capabilities. Because of these factors, Ofgem believes these parties are best suited to carry out market making. We disagree with this logic.

For effective market making, we believe that the market maker needs to base its pricing purely on its belief as to the prices it will be able to buy and sell products. Market making has nothing to do with own production. We therefore question whether it would be appropriate that the market maker could price in the knowledge that it can absorb a long position or produce to cover a short position. Even if it is deemed appropriate to have such capabilities, these would only be available if its supply and generation businesses did not hedge until after all market making product timeframes had closed. We therefore question how a presence in the domestic supply market and being in more than one point on the vertical supply chains of electricity and gas can aid a company in making bids and offers for specific products, as has been suggested by Ofgem.



If the market making is being carried out by an independent third party (the Nominee), to overcome the issues associated with MiFID II, then unless an inside trading arrangement is secured with the Relevant Licensee and an associated supply licensee:

1. the obligated organisation's presence in the domestic market becomes irrelevant to the market maker;
2. any self supply by the obligated organisation is not relevant as to how the market maker operates; and
3. any trading capability the obligated organisation has for market making will be lost, due to it no longer being in a position to market make.

In summary, once an independent third party (Nominee) has to be used to carry out market making, due to European regulations, Ofgem's reasons for particular generation licensees to market make, or procure the services of a third party market maker, are no longer valid. The Relevant Licensee is in the same situation as any other organisation with a generation licensee within its group. To place an obligation on a particular generation licensee to provide market making, or its provision, when it is not practicable for it to provide such a service would be discriminatory.

A further complication is that the current drafting of the Market Access service means that this service has to be provided at below cost. Those providing the service will be subsidising the rest of the market, including their competitors. With such subsidies being provided, the cost of that subsidy needs to be fairly distributed across all suppliers, not eight corporate groups. Not to do so would be discriminatory against the Relevant Licensees. Fair distribution of the costs would also better reflect Ofgem's apparent objective of introducing market making to support all suppliers.

Rather than having discriminatory arrangements, or the complications of smearing the costs of subsidies across all suppliers, the licence obligation should facilitate those providing the services cover their costs and be able to make a fair return. To achieve this:

1. the provider of the Market Access service should be able to pass through all incremental costs, including any administrative charge and other internal costs incurred;
2. the incorporation of an option fee in the quoted price should be permitted in the rules controlling the Market Access service, so as to cover the risk of market price changes between offers being made to Eligible Suppliers and the Eligible Supplier exercising the option; and
3. the price regulation of the Market Making service, through controls on bid offer spreads, should be set sufficiently wide that market makers can have a reasonable expectation of covering their costs and of securing profits that reflect the financial risks they will be exposed to.



While there is a clear need for an option fee for the Market Access services, the cost of not having such a fee is heightened if the proposed windows trading for the Market Making service is introduced. Having windows based market making risks concentrating market liquidity in the window periods with a corresponding illiquid market outside of the window periods. If this occurs, those having to provide the Market Access service are exposed to giving prices based on high liquidity periods (window periods) but having to procure to back exercised options during illiquid periods. The obligated parties will be very exposed to Eligible Suppliers arbitraging between liquid and illiquid periods of the market.

In our response to Ofgem's "Wholesale power market liquidity: final proposals for a 'Secure and Promote' licence condition and Draft Impact Assessment" we explained that Ofgem was proposing caps on each market maker's bid offer spreads. This would effectively introducing price regulation of market making in the Great Britain wholesale power market. Further, these price regulated caps for each market maker seemed to be much tighter than the bid offer spreads typically seen in many other markets.

Besides risking unintended consequences for the market as a whole, by setting tight caps on bid offer spreads for individual market makers, Ofgem would make it more difficult for market makers to cover their costs. With limited potential to cover costs, retaining tight bid offer spreads would require subsidies from the industry, the costs of which would inevitably feed through to customers. It would also make it harder to attract independent third party market makers into the market.

We explained that if there was genuine use of the market making by industry participants, rather than just market makers circulating very small volumes to achieve low cost compliance, the market spreads would usually be much tighter than the maximums permitted.

We also explained that while Ofgem was proposing that the cap on bid offer spreads would be set as a percentage, this was different to the usual fixed monetary value. Market makers needed to be able to cover costs and therefore required a fixed monetary value so as to secure the necessary income at times of low prices. Fixed spreads would also simplify the market making process.

Based on E.ON Global Commodities experience in Europe, and their requirements for providing market making services, if market makers were not to require subsidies from licensees, we recommended that any regulatory cap on bid offer spreads for individual market makers was as set out in Table 1 below.



Table 1 - Possible maximum bid offer spreads for individual market makers

	Baseload	Peak
	Index linked	Index Linked
Month+1	£1.20/MWh	£2.40/MWh
Month+2	£1.20/MWh	£2.40/MWh
Quarter+1	60p/MWh	£1.20/MWh
Season+1	30p/MWh	60p/MWh
Season+2	30p/MWh	60p/MWh
Season+3	30p/MWh	60p/MWh
Season+4	30p/MWh	N/A

The structure of the regulated cap on maximum permitted spreads, shown in Table 1 above, was to reflect that for the market maker:

1. The products covering longer periods could have smaller maximum spreads as there was a larger volume over which costs could be recovered;
2. Baseload could have smaller spreads for the same time period than peak, again because there was a greater volume over which costs could be recovered;
3. The products that covered longer periods could have smaller maximum spreads through term structure of volatility, because the risks of volatility were more predictable for the long period products than the short period products;
4. There was sufficient spread to allow for unforeseen changes in the market after the limits were set; and
5. This was an imposed market making obligation that could not be exited, unlike voluntary market making, which can be exited.

We note that Ofgem's final proposals do not reflect our above observations. However, we remain of the opinion that our comments above are valid.

The impractical nature of the obligations

The proposed licence condition sets a number of obligations where compliance will not be possible. For example, paragraph 6 of Schedule B requires that "*Bids and offers for each Product must be posted on a qualifying platform at all times (subject to paragraph (b)) in the periods of 60 minutes (each a "trading window") starting respectively at 10.30 hours and 15.30 hours every working day.*" Without some flexibility on the lines of paragraph 5 of Schedule A with its "*the licensee shall take all reasonable steps to ...*",



Relevant Licensees cannot guarantee that they will do certain actions “at all times”; for example, there could be an IT failure at that time, or the party providing the bids and offers has to evacuate its building due to a fire alarm. The absolute requirements to carry out positive operational actions, such as making bids and offers available, is unreasonable and needs modifying so as to reflect the reality that carrying out positive operational actions must be based on taking reasonable steps to secure delivery of compliance.

Ofgem’s “Enforcement Guidelines on Complaints and Investigations” do not offer a form of protection against breaching the licence condition, just an assurance that Ofgem will follow its usual enforcement guidelines when deciding whether to take action. However, it has been suggested that such flexibility as having “taking reasonable steps” within the proposed licence condition is not required, because Ofgem’s Enforcement Guidelines on Complaints and Investigations means that breaches of the licence, due to events that taking reasonable steps could not prevent, are unlikely to attract enforcement action. Such an arrangement is totally unacceptable. At a time when the industry and Ofgem is trying to restore customer confidence;

1. how will stories of breaches of licences support trust in the licensees? and
2. how will stories of breaches of licences not being punished by Ofgem support trust in Ofgem?

Also, corporate groups, such as E.ON, take compliance with regulations extremely seriously. How can we strive for getting things right and, at the same time, have to introduce procedures and policies that we know cannot be complied with? For example, introducing a rule that the IT system will not fail “*in the periods of 60 minutes (each a “trading window”) starting respectively at 10.30 hours and 15.30 hours every working day*”⁹?

Normal market making contracts between market makers and exchanges carry force majeure clauses. These are there to recognise the practical issues in committing to carrying out positive operational actions. We accept that a force majeure clause would be difficult for a licence condition, but ask that the problem is recognised and addressed by the licence requiring that “the licensee shall take all reasonable steps to...”.

From a risk management perspective, Ofgem’s Enforcement Guidelines on Complaints and Investigations are only guidelines. These guidelines can change and Ofgem is free to adopt a zero tolerance on licence compliance. In accepting the proposed licence condition, what assurance would the Relevant Licensees have that Ofgem would never take enforcement action for breaches of the licence where the Relevant Licensee had

⁹ Wholesale power market liquidity: final proposals for a 'Secure and Promote' licence condition June 2013 Appendix 2, Schedule 2, Schedule B, paragraph 6(a).



taken reasonable steps to achieve compliance? Such assurance can only be achieved if the licence sets that licensee shall take all reasonable steps to deliver compliance.

E.ON's Code of Conduct, which is applicable to all E.ON employees, is very clear that, *"The legal framework for our activities must be observed without fail. That also applies to our internal policies, which give substance to the respective laws and regulations and to our ethical principles. This remains fully valid: Infringements will not be accepted; we would rather abandon business deals and internal targets than violate laws or policies. No supervisor is allowed to issue instructions to the contrary or to tolerate any infringements"*. It is difficult to see how, with such a policy, E.ON can accept licence conditions that have absolute requirements to carry out positive operational actions.

The criteria for a licensee being captured under this licence condition

The current drafting of the Liquidity in the Wholesale Electricity Market licence condition is likely to impose costs on the obligated licences that they may not be able to recover. If this happens the Relevant Licensees will be subsidising their competitors. Having to provide a non-recoverable subsidy devalues a company's worth.

Ofgem has recognised this issue in its Draft Guidance, stating that *"where an S&P licensee sells a specific asset including the associated generation licence with an S&P licence condition to a non-S&P licensee, we will normally disapply the S&P licence condition through a direction from the Authority. In straightforward cases, this process should be relatively quick."*¹⁰ However, this is not a guarantee that the licence condition will be removed from a Relevant Licensee, should the corporate group sell it. Any attempted sale will be subject to an Ofgem decision to remove the licence condition from that licensee. This will make such a sale more difficult and so devalue the attractiveness of that Relevant Licensee to the market and thus its potential sale value.

This issue can be easily be overcome if the proposed licence condition is made a "standard licence condition" and there is a strict criterion within the licence as to when a licensee qualifies as a Relevant Licensee, in the same way that Relevant Licensees are defined in the Generation Licence Condition 16B, *Financial Information Reporting*. With such a simple, clear and much less discriminatory criterion, the current commentary in the Guidance could be withdrawn.

Failure to have clear thresholds as to when a licensee becomes a Relevant Licensee under the proposed licence condition raises the charge that Ofgem is discriminating against certain licensees.

¹⁰ Liquidity: in the Wholesale Electricity Market (Special Condition AA of the electricity generation licence): Draft Guidance paragraph 1.16.



MiFID II and EMIR

Ofgem has recognised the concerns surrounding European Financial Regulations, by allowing the Relevant Licensees to use Nominees to provide the market making service for it. This permits a means by which the Relevant Licensee can comply with the obligations of providing the Market Making service without being caught under MiFID II or EMIR. However, the Relevant Licensee may not be able to procure the services of a Nominee without being materially and adversely affected.

To remove what would be a very significant risk for the Relevant Licensees, protection for the Relevant Licensee is needed. Therefore, where a Relevant Licensee can show that to carry out the Market Making service by itself, or by an affiliate, would have material adverse consequences for its corporate group and that, having taken all reasonable steps to secure the services of a Nominee, it has not been able to secure those services, the requirements for it to provide the Market Making service should be suspended until an appropriate solution can be found.

The protection currently offered in paragraph 11 of Schedule B is that *"Where the licensee considers that any amendment or replacement of MiFID or EMIR may materially and adversely affect the ability of the licensee to comply with this Schedule B, the licensee may submit to the Authority a request (which for the avoidance of doubt shall not bind the Authority) to undertake a review of the provisions of Schedule B"*. This does not provide sufficient protection to the Relevant Licensees. To mitigate the uncertainty over European financial legislation, paragraph 11 of Schedule B should be based on delivering the Market Making services only when it is reasonable to provide the service either:

1. by the Relevant Licensee's corporate group; or
2. through the use of a Nominee.

Timetable for implementation

Notwithstanding our concerns, the provision of Market Access services and price regulated Market Making services will be new to most of the Relevant Licensees and their corporate groups. We assume that the licence conditions can still be modified, before coming into effect, and so become acceptable to potential Relevant Licensees. Based on this assumption, E.ON's Relevant Licensees have opened discussions with a third party provider, E.ON Global Commodities (EGC), for the provision of the two services and the reporting. In response EGC has stated that it will require 90 days notice to introduce the new services.

Based on a 90 days notice, we ask that the requirements of the licence condition are not brought into effect until 130 days after Ofgem's decision is announced. The 130 days is the 90 days for development plus 40 days. The 40 days is the time between the decision being announced and a contractual commitment between the Relevant



Licensees and their providers being signed. This covers the time between Ofgem announcing its decision, any appeals to the Competition Commission being made and the Competition Commission declining to hear the appeal.

If the Relevant Licensees cannot use third parties then they will need significantly more time than 90 days to prepare. In this situation we would ask that the requirements of the licence condition are not brought into effect until 300 days after Ofgem's decision is announced.

5. E.ON's comments on the detail of Ofgem's proposed Liquidity in the Wholesale Electricity Market licence condition

Licence Condition Paragraph	Issue	Possible solution
Para AA.2	The proposed licence condition refers only to the licensee, suggesting that E.ON has to provide this service five times. The guidance says "Our 'Secure and Promote' (S&P) policy is being introduced through a special condition, inserted into all generation licences held by certain company groups. (For the avoidance of doubt, the obligation only needs to be met once by each group)."	The principles of paragraph 3 of Condition 16B are adapted so that "The licensee shall, in conjunction with any Affiliates that are Relevant Licensees, with effect from such date or dates as the Authority may specify in a direction given to the Licensee:" <u>and</u> The Guidance is made clear that the requirements of Schedules A, B and C for Relevant Licensees that are Affiliates of each other can be complied with as if the Affiliates were a single entity.
General for Schedules A and C	Schedules A and C refer to actions by the Licensee, but Schedule B allows the use of Nominees. This suggests that third parties cannot be used to deliver the obligations of Schedules A and C.	The Guidance is made clear that licensees can use third parties to deliver all of the licence condition's obligations.
Para AA.3	This paragraph is unclear. Will it apply to E.ON's generation licensees? If it does, what happens if the licensee does not give its consent?	Redrafting of paragraph AA.3, or a clear explanation is provided in the Guidance.
Para AA.5	The licence condition does not have qualifying criteria for which licensees become Relevant Licensees.	Incorporate the principles of paragraph 8 of Condition 16B (Relevant Licensee), which sets out qualifying criteria.
Schedule A Para 2, 3, 6, 8, 9, 10, 12	The paragraphs have the licensee "must". There are no provisions for events where the licensee cannot, for legal or technical reasons, meet the obligation.	Replace "the licensee must" with "the licensee must take all reasonable steps to"

Licence Condition Paragraph	Issue	Possible solution
Schedule A Para 5, 7, 11	The paragraphs have the licensee "shall" in a number of situations. There are no provisions to cover events where the licensee cannot, for legal or technical reasons, meet the obligation.	Replace "shall" with "the licensee shall take all reasonable steps to"
Schedule A Para 4	It is not clear if the trading agreements have to be between the Eligible Supplier and the licensee, or between the Eligible Supplier and another party, which is contracted by the licensee.	The Guidance to be clear that licensees can use third parties for the trading agreements with Eligible Suppliers.
Schedule A Para 4	There is no flexibility around the written response, but the Guidance says "we expect licensees to have due regard to other regulations that they are subject to"	Redrafting of paragraph 4 to "Subject to the requirement of other regulations the written response must include"
Schedule A Para 9	It is not clear that credit terms in the trading agreements can be flexible and change over time, which they need to.	The Guidance to be made clear that trading agreements' credit terms can be flexible and change over time.
Schedule A Para 9	It is not clear that the Trading Agreements with Eligible Suppliers will be different to the standard trading agreements currently used.	The Guidance to be clear that Trading Agreements for Eligible Suppliers will be different to standard Trading Agreements used elsewhere in the wholesale power market.
Schedule A Para 11	Most of E.ON's generation licensees do not have their own website.	Incorporate into the licence paragraph 8 of Condition 16B (Website), which gives more flexibility.
Schedule A Para 12	There are no exceptions as to when a request to quote can be declined.	Redrafting of paragraph 12 to incorporate; "the licensee shall take all reasonable steps to secure the provision of a quote in response to a qualifying request to trade:"

Licence Condition Paragraph	Issue	Possible solution
Schedule A Para 13	The licensees will be quoting against prices that may not be available to the licensee by the time the Eligible Supplier accepts.	Redraft paragraph 15 to include; "a charge which is a reasonable reflection of the risk incurred by allowing a time between the licensee's quote and the Eligible Supplier acceptance."
Schedule A Para 15	It is not clear that licensee does not have to have direct access to the market.	The Guidance should be clear that licensees can use third parties for accessing the market and that the market price to the licensee is the price provided to the licensee by the third party.
Schedule A Para 15	Because the current drafting of the licence sets out that licensee may not include any administrative charge or any other internal costs incurred as a result of trading with the Eligible Supplier, it will not be able to cover the cost of providing this service.	Redraft paragraph 15 to include; "The licensee may include a charge that is a reasonable reflection of any internal costs incurred as a result of trading with the Eligible Supplier"
Schedule A Para 16	The current definition of Trading Agreement is vague and does not differentiate between normal trading agreements and those specifically for Eligible Suppliers.	A more detailed definition is required.
Schedule A Para 16	As defined the working day will default to every day.	A more detailed definition is required.
Schedule B Para 2	The paragraph has the licensee "shall" with no provisions to cover events where the licensee cannot, for legal or technical reasons, meet the obligation.	Replace "shall" with "the licensee shall take all reasonable steps to"
Schedule B Para 2, 3	The current drafting only refers to the licensee, when it could be the licensee or its Nominee.	Change "licensee" to "licensee or Nominee"

Licence Condition Paragraph	Issue	Possible solution
Schedule B Para 4b,6a and 6b	The paragraphs have "must" with no provisions to cover events where the licensee cannot, for legal or technical reasons, meet the obligation.	Replace "must" with "the licensee must take all reasonable steps to"
Schedule B Para 4c, 9	E.ON has five generation licensees. The current drafting suggests that it will have to finance the operation of at least three market makers.	Modify 4.c.(1), 4.c. (ii) and 9.(b) to "Relevant Licensees, other than Affiliates of the Licensee that are Relevant Licensees,"
Schedule B Para 4b	<p>The drafting is unclear suggesting that the licensee must use a Nominee; or that Nominees have more exact trading requirements than Licensees.</p> <p>Also, the current drafting does not accommodate exchange based trading, where the trade is with the exchange.</p>	<p>Modify 4b to "The Licensee, or its Nominee, must take all reasonable steps to secure that at all times there are arrangements in place to trade such Product(s) on any qualifying platform where there are at least 5 other persons able to trade who are not affiliates of the Licensee or the Nominee."</p> <p>The Guidance to make it clear that the requirement is that the Licensee or its Nominee must take all reasonable steps to secure that at all times there are arrangements in place to support trading with at least 5 other persons, who are not affiliates of the licensee or the Nominee, to trade such Product(s) on any qualifying platform. Also, that an exchange with more than five participants is deemed to support trading with at least 5 other persons.</p>

Licence Condition Paragraph	Issue	Possible solution
Schedule B Para 4c	As E.ON has five generation licensees, the drafting suggests that it will have to establish, or secure the services of three Nominees.	Add clarification to the Guidance and modify paragraph 4c so that "The licensee may not nominate a person as Nominee in relation to a month if that person is also nominated as Nominee in relation to that month: (i) by two other Relevant Licensees, other than Affiliates of the licensee, or (ii) if the Nominee is itself a Relevant Licensee, other than an affiliate of the licensee, or an affiliate of a Relevant Licensee, other than an Affiliate of the licensee, by one other Relevant Licensee, other than an Affiliate of the licensee."
Schedule B Para 6a	Window trading with price regulated market making risks removing liquidity from the rest of the market.	Having market making across the working day would overcome this problem.
Schedule B Para 6a	Working day is referred to, but Schedule B does not have a definition of the working day.	The definition of working day developed for Schedule A should also be used in Schedule B.
Schedule B Para 8	This introduces price regulation to wholesale market's market making with the risk that the regulated price is below cost.	Set the regulated prices for the bid offer spread sufficiently wide that the provider can make an appropriate profit, as per other price regulation.
	The price regulated bid offer spreads widen further out on the curve, while the risk decreases further out on the curve.	The price regulated bid offer spreads should tighten out along the curve.

Licence Condition Paragraph	Issue	Possible solution
Schedule B Para 8	The current drafting suggests that the price regulated bid offer spreads apply to all bids and offers posted by the licensee, not just the regulated 5MW and 10MW blocks.	The Guidance to be clear that the regulation of bid offer spreads only applies to the regulated market making products and the regulated volumes of those market making products. Also, that all trading outside of the regulated volumes of the regulated market making products can have any bid offer spread.
Schedule B Para 11	This does not give Relevant Licensees appropriate protection from MiFID II or EMIR, where there are potentially very high costs for corporate groups. Nor does it give protection from any other market making related rules, which would impose costs on a Relevant Licensee.	Modify the paragraph so that if the licensee has taken all reasonable steps to secure the services of a Nominee, but has not been able to secure the services of such a Nominee, in such a situation the requirements to provide Market Making services are suspended until an appropriate solution can be found.
Schedule C Para 1	The Guidance paragraph 4.7 states that "the licensee or their nominated third party will have to submit to Ofgem a quarterly report", but Schedule C only refers to the licensee.	Redraft paragraph 1 to "The licensee must take all reasonable steps to secure the submission of a report."
Schedule C Information Table Column Schedule A	Reporting of "total aggregate volume of each Product bought and sold with Eligible Suppliers" means the reporting of forward looking and thus commercially sensitive information.	The guidance must be very clear that information that is forward looking will be treated in strictest confidence, with no publishing of such information.
Schedule C Information Table	It is not clear what is meant by "Gross volumes bought and sold through day-ahead auctions each month".	A definition in the licence is required, or a detailed explanation in the Guidance.