

Ofgem
Attention: Graham Knowles
9 Millbank
London
United Kingdom

2 August 2013

Dear Graham

APX response to Ofgem call for evidence on price benchmarks

On the 1 March 2013 APX-ENDEX split into a power spot and clearing entity (APX) and a derivatives and spot gas entity (ICE-ENDEX). APX operates prompt, auction and intraday (near to real time) markets in the United Kingdom, Netherlands and Belgium. The split has allowed a renewed focus of APX on the operation and development of efficient and interconnected close to real time power markets.

As part of this renewed focus we held our first APX Market Development Advisory Board (MDAB) meeting for the United Kingdom on the 27 June. We took the decision to establish both a UK and continental MDAB, instead of a single MDAB for all markets, to better reflect the specific challenges that APX and our members face.

APX Response Summary

We understand that Ofgem is primarily seeking feedback on how price benchmarks are used by the market. In our response we explain the price benchmarks that APX provide and our understanding of their use by market participants. In particular we focus on APX's role in setting the GB Market Index Price.

We are happy to respond to Ofgem's call for evidence. However, we wish to understand how Ofgem will use the information provided. We hope that a better understanding of price benchmarks will be used to inform Ofgem and DECC's regulatory initiatives.

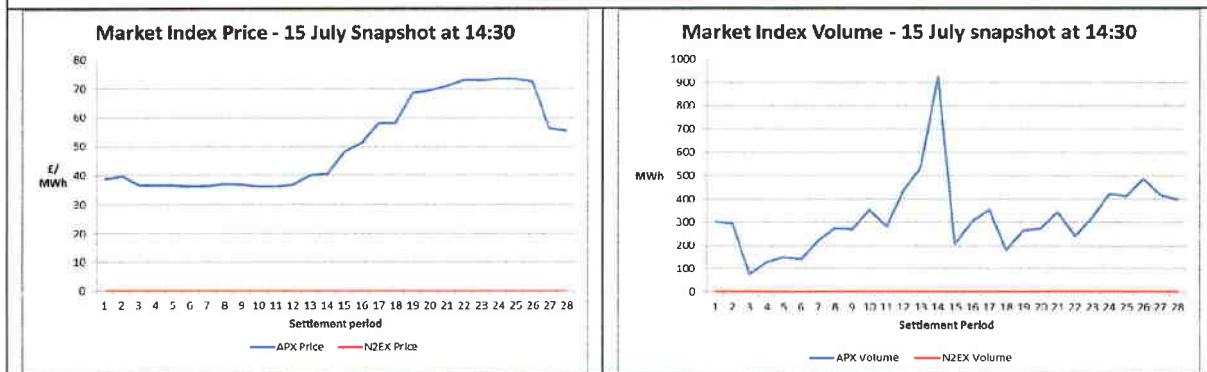
APX as the GB Market Index Data Provider

APX and N2EX are registered to provide Market Index Data to Elexon. Elexon use the Market Index Data to calculate the Reverse Price for cash-out in the GB settlement process. The Reverse Price is calculated to reflect the wholesale price of electricity just before Gate Closure.

Close to real time data on the Market Index Price and Volume is published on the Elexon Balancing Mechanism Reporting System¹. The two graphs below provide a snapshot of the Market Index Price and Volume data submitted by APX and N2EX on 15 July:

¹ <http://www.bmreports.com/>

Snapshot of GB Market Index Price and Volumes



All contracts in GB are traded against the last price in the market as this is the point at which the market has the most information about fundamentals. Therefore, the Market Index Price currently acts as the main GB price benchmark for electricity.

Elexon publishes an Imbalance Price Guide². This provides detailed information on how the Market Index Price is used in imbalance settlement. Elexon also publishes a Market Index Definition Statement (MIDS)³ as required by Section T of the Balancing and Settlement Code (BSC). The MIDS contains the following information:

- (a) Market Index Data Provider(s) details
- (b) Full definition of the particular data and methodology (time and product weightings) to be used by the Market Index Data Provider(s) in determining the Market Index Data for each Settlement Period
- (c) Individual liquidity thresholds for each Market Index Data Provider

The MIDS is reviewed by the BSC Panel at least once a year. Any proposed changes are consulted upon with BSC Parties and other interested Parties before the BSC Panel determines that a change is to be made. A change to the MIDS is subject to approval by Ofgem.

This is an example of a price benchmark which is regulated by Ofgem. Some elements of cash-out are currently under review in Ofgem's Electricity Balancing Significant Code Review.

APX reference price data

APX publish historical reference price data for our GB spot and auction markets⁴. This is in addition to the Market Index Data that APX provide for Elexon to calculate and publish the GB Market Index Price and Volume. APX reference price data is free to download on our website. We do not charge for the provision of this information or restrict access to non-members.

The methodologies used by APX to calculate historical reference price are also published on our website⁵. The reference price data include estimates of:

- **APX UK Base:** volume-weighted reference price for each half hour settlement period each day where such data is available between 23.00 and 23.00 UK local time

² http://www.elexon.co.uk/wp-content/uploads/2013/02/imbalance_pricing_guidance_v4.0.pdf

³ http://www.elexon.co.uk/wp-content/uploads/2012/01/mids_v7.0.pdf

⁴ <http://www.apxgroup.com/market-results/apx-power-uk/ukpx-rpd-historical-data/>

⁵ <http://www.apxgroup.com/market-results/apx-power-uk/ukpx-rpd-index-methodology/>

APX Commodities Limited / Registered in England and Wales No 3751681 / VAT registration: GB-728 4155 27

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- **APX UK Industrial Peak:** volume-weighted reference price for each half hour settlement period each day between 07:00 and 19:00 UK local time
- **APX UK Extended Peak:** volume-weighted reference price for each half hour settlement period each day between 07:00 and 23:00 UK local time
- **APX UK Off Peak:** volume-weighted reference price for each half hour settlement period each day where between 23:00 and 07:00 & 19:00 and 23:00 UK local time

The reference price data are based on trades that have been concluded on APX markets in the UK. APX also publish reference price data based on the results of our day-ahead auction. The historical data is made available for a period from 2001 to present.

The link between near term prices and forwards

Near terms price benchmarks are used by market participants in any calculation that requires shape to be added to forward prices. Forward prices are generally for either baseload or peaking contracts. However, the demand for electricity and its price will change significantly throughout the day. Anticipated changes in prices depend on many factors, such as the season, or whether coal or gas is acting as the marginal plant.

To add shape, market participants use models and historic near term prices to add shape to baseload or peaking forward prices. We understand that the Market Index Price and other APX price indices are used for the following calculations:

- When seeking to calculate Value at Risk on forward positions. The Value at Risk is used in annual accounts as part of a market participants IAS39 submission and embedded in their IAS39 reporting methodology.
- Calculation of Value at Risk on forward positions is also used to calculate credit positions on which a Partial Credit Guarantees or Letters of Credit will be sought or purchased.
- To value structure contracts such as tolling agreements or those with within day flexibility.
- To plan outages for generation plant, to assess whether flexible plant should be maintained or mothballed and as part of investment decisions in new plant or to approximate the value in the acquisition of new plant
- For internal transfer pricing between supply and generation to ensure correct costs are passed between the different legs of a vertically integrated market participant
- To shape products for retail customers using the standard load profiles and to price half hourly metered I&C customer profiles

The Market Index Price and APX price indices are also used as an acceptable substitute for GB Pool prices where they are still referenced in old contracts.

Regulatory policy that affects price benchmarks

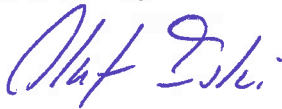
As Ofgem notes in its call for evidence there is considerable regulatory interest in promoting robust, reliable and transparent price benchmarks and reduce the scope for manipulation. Key

regulatory initiatives that will impact on GB benchmark prices include Ofgem's liquidity project and electricity balancing significant code review, DECC's electricity market reform the implementation of REMIT and proposed EU regulation on price benchmarks.

We propose that Ofgem organise a roundtable to discuss the conclusions of this call for evidence as well as to discuss the anticipated impact of the proposed EU regulation of price benchmarks in GB.

Please do not hesitate to contact me if there is any aspect of this response that you would like to discuss further.

Yours sincerely,



Olaf Islei
Public and Regulatory Affairs



ANNEX 1 – Snapshot of Market Index Price Data for 15 July at 14.30

Settlement Period	N2EX Price	N2EX Volume	APX Price	APX Volume
1	0	0	38.76	303
2	0	0	39.86	296.5
3	0	0	36.67	76
4	0	0	36.6	129.65
5	0	0	36.62	151.5
6	0	0	36.3	141.5
7	0	0	36.42	221
8	0	0	37.03	275
9	0	0	36.75	271.5
10	0	0	36.15	354.55
11	0	0	36.33	283
12	0	0	36.89	438
13	0	0	40.25	534.1
14	0	0	40.64	924.3
15	0	0	48.31	207
16	0	0	51.27	306.1
17	0	0	58.08	354.85
18	0	0	58.14	179.7
19	0	0	68.48	267
20	0	0	69.36	274.05
21	0	0	70.87	344.65
22	0	0	72.96	242.35
23	0	0	72.91	319.95
24	0	0	73.34	422.65
25	0	0	73.47	412.65
26	0	0	72.39	486.4
27	0	0	56.27	417.8
28	0	0	55.52	397.45

