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Dear Mr Knowles,

Pricing benchmarks in gas and electricity markets - a call for evidence

I am writing on behalf of Argus Media to respond to Ofgem's call for evidence issued on 6 June.

We thank you for the positive terms in which Ofgem refers to the assistance that the price reporting agencies (PRAs) provided to Ofgem in preparing its call for evidence and, like Ofgem, we would welcome "*further constructive engagement... going forward*". We note the evident care that Ofgem has taken in considering this subject, which has led to some very perceptive and helpful analysis, particularly in relation to the potential dangers of certain types of regulation that can produce negative results.

Chapter 1 Introduction:

Although the call for evidence does not ask any questions in regard to chapter 1, we believe it may be worthwhile to summarise developments that have taken place since the call for evidence was published, and which are relevant to the section in chapter 1 entitled "*The Broader Landscape*".

- **Section 1.4: The G20 Agenda:**

On 17th July, IOSCO issued its *Final Report on its Principles for Financial Benchmarks*¹. There had been some speculation that these new IOSCO principles might modify or even supersede the PRA Principles². However, IOSCO's new *Final Report* forcefully reaffirms the PRA Principles and also distinguishes them from IOSCO's more generalised new principles in the following terms:

"Specific Application for Oil PRAs

In October 2012, IOSCO adopted the PRA Principles, which were developed in collaboration with the International Energy Agency (IEA), International Energy Forum (IEF), and the Organization of Petroleum Exporting Countries (OPEC). IOSCO recommended voluntary

¹ IOSCO FR07/13

² IOSCO FR06/12, Principles for Oil Price Reporting Agencies, Final Report

adoption and implementation of the PRA Principles and established a review process over the 18 months following their publication, pursuant to which IOSCO, in collaboration with the IEA, IEF and OPEC, will evaluate the degree to which the PRA Principles have been implemented by PRAs. IOSCO further stated that it will seek the input of market authorities, stakeholders and PRAs and make further recommendations as appropriate at the end of the evaluation period.

As noted above, IOSCO took into consideration the PRA Principles during the development of these Principles for Financial Benchmarks. Moreover, the PRA Principles were developed with due regard to the specifics of the oil markets, while these Principles for Financial Benchmarks focus on Benchmarks generally. As a result, while both sets of principles reflect similar high-level concerns, they differ in specifics.

In order to respect the circumstances under which these two sets of principles have been adopted, as well as the on-going evaluation process of the PRA Principles, IOSCO expects that the oil PRAs should continue to comply with and implement the PRA Principles.

IOSCO will, in the context of its collaboration with the IEA, IEF and OPEC, consider the need in due course for any modification of the PRA Principles to align them more closely with these Principles for Financial Benchmarks.”

- **Section 1.5: The ESMA/EBA Agenda:**

On 6th June, the same date on which Ofgem published its call for evidence, ESMA and the EBA issued their “*Principles for Benchmark-Setting Processes in the EU*”³. The introduction clarified that the ESMA-EBA principles are “*without prejudice to the IOSCO Principles for Oil Price Reporting Agencies*”.

- **Section 1.6: The Market Abuse Regulation (MAR):**

Argus Media supports the extension of the scope of the EU’s draft Market Abuse Regulation (MAR) to manipulating benchmarks. Along with the existing prohibitions in REMIT, we consider that these provide an effective regime that clearly prohibits any manipulation of benchmarks and provides for strong deterrent sanctions. We fully support this as an important safeguard to the integrity of our published price assessments.

Unfortunately, the initial drafting of MAR’s Article 8.1.d did not align with the approach taken by MAR towards the other categories of manipulation already covered in Article 8. These included a “*knew or ought to have known*” proviso to allow for honest mistakes, as is also the case in the US Dodd-Frank legislation⁴. Likewise, and as is recorded by Ofgem⁵, REMIT requires intent for there to be manipulation. By contrast, MAR 8.1.d as originally drafted imposes strict liability in the case of benchmarks, with no allowance for honest mistakes. Such an unreasonable and disproportionate regime would inevitably discourage the voluntary provision of market data by market sources to PRA journalists. We have been working with HM Treasury and others to try to align the drafting of Article

³ ESMA/2013/659

⁴ Section 753 of Dodd-Frank Wall Street Reform And Consumer Protection Act

⁵ Ofgem call for evidence, section 2.11

8.1.d with the other provisions in MAR, and to avoid penalising honest mistakes by market sources. At the date of writing, the final position on Article 8.1.d unfortunately remains unclear.

Question 1: Do you agree with our review of the issues?

We welcome the clear, well-balanced, evidence-based approach that Ofgem has taken in chapter 2 including:

- The brief summary of the journalistic processes that underlie a PRA price assessment⁶;
- The recognition that PRAs operate in a competitive environment and “*may be deemed to have a commercial incentive to ensure that their customers retain confidence in their products*”⁷;
- The contrasts made between Libor and PRA benchmarking processes and the conclusion that there is lower risk profile in the latter⁸; and
- The references to the European anti-abuse frameworks of REMIT and MAR⁹.

In addition, we would like to single out as particularly welcome, the section “*Forming a benchmark price*” in paragraphs 2.16-2.22, including the two illustrations. We have read no comparable analysis of the impacts of regulation on the information flows that are essential for well-functioning energy markets or guidance on the types of regulation that can produce positive but also negative impacts.

Sections 2.19 and 2.21 are especially apposite:

“...some types of regulation may also introduce risks to the process. In particular, greater regulatory scrutiny of the information flows could introduce a perception of risk (irrespective of whether the risk is real) to those providing the information. Regulation should increase the quality of the information provided, but could reduce the willingness of parties to provide it. Information is provided on a voluntary basis and the simplest way to mitigate this risk may be to withdraw cooperation and decline to provide it. This in turn can lead to a breakdown in the quality of the price assessment process, with negative consequences for the market and for consumers.”

“Good information is essential for a well functioning market. It is therefore very important for both regulators and market participants alike to consider this relationship and ensure that the market continues to have good quality information available.”

Ofgem’s analysis reinforces and expands on IOSCO’s warning in its Final Report on Principles for Oil Price Reporting Agencies:

⁶ Ofgem call for evidence, section 2.15

⁷ Ofgem call for evidence, sections 2.22 and 2.23

⁸ Ofgem call for evidence, note 9

⁹ Ofgem call for evidence, sections 2.10, 2.11 and note 13

“It is important to understand that these principles recognize that there is no requirement on any physical market oil participant to submit transaction data to PRAs. Because data are submitted on a voluntary basis, precipitous regulation of PRAs or requirements that oil market participants who submit data to PRAs submit all of their transaction data potentially could result in some oil market participants to decrease or even cease their submission of data to PRAs”¹⁰

Unfortunately, there is not always sufficient awareness among policy-makers about the differences that exist between benchmarking processes in pure financial markets and those in physical commodity markets, and the risks to the latter from applying regulation that has been designed for the former. In this context, we welcome the approach that Ofgem outlines:

“We are mindful that any action might come with unintended consequences and that we would need to work with stakeholders to identify and mitigate these.”¹¹

The dangers of regulators proceeding without engagement with stakeholders are exemplified clearly in DG MARKT’s draft European regulation on benchmarks, recently placed in inter service consultation in Brussels. Its approach does not appear to have been informed by any impact assessments or engagement with stakeholders in respect of energy markets and benchmarks. Nor is it aligned with the recommendations of Ofgem or IOSCO. As a result, it poses threats to Europe’s energy markets.

We would like to offer comment on section 2.5 of the call for evidence, which notes that allegations have been made in the UK national press as regards one particular PRA. Argus Media is not in a position to comment on those specific allegations as they do not relate to Argus Media. However, in respect of our own operations, we would note that the UK operations of Argus Media have been accredited for over a decade by the UK government’s Investors in People programme, a certification which recognises the quality and commitment to staff selection, training and development, as well as internal communications. This accreditation has just been subject to external review and has been re-awarded for a further three years. All our staff are subject to rigorous recruitment procedures, which in the case of market reporting staff includes testing during recruitment that simulates and assesses the ability to acquire the skills necessary in market reporting or to confirm such skills. All our market reporting staff undergo extensive initial training prior to commencing market reporting. This is followed by an extended period of coaching, support and mentoring supervision by experienced editorial staff as junior staff commence reporting on markets. Argus Media expects the highest standards of journalistic market reporting and takes steps to ensure such standards are met including by maintaining an ongoing review of the work of its editorial staff. Our staff are monitored and mentored by their supervisors, and the abilities of market reporters are subject to continuous review through daily interaction with editors. All junior staff and new joiners are reviewed formally at least twice a year and senior staff are appraised on an annual basis. Reviews are standardised for editorial staff in each role (eg market reporter) to help ensure the consistency of staff quality across all assessed markets. Senior editorial managers review monthly reports on correction rates and other employee performance data.

¹⁰ IOSCO FR06/12, pages 8 and 34

¹¹ Ofgem call for evidence, section 3.5

As regards application of methodologies, all Argus Media market reporters are required to rigorously follow methodologies, and are given the necessary training, support and supervision to ensure this in practice. Argus Media operates all its market reporting activities within a rigorous controls framework. Processes are closely supervised by editors and senior managers, with any failure to follow a methodology considered a serious disciplinary offence subject to sanction including up to dismissal. In addition, regular internal audits are carried out by the company's Global Compliance Manager to independently verify that methodologies, policies and procedures are being fully and consistently observed. A key test under these internal audits is to be able to recreate a published price on any day from all the gathered inputs and strictly following the relevant methodology.

We would also note that all signatories to the now-finalised IPRO Code (discussed further below) have committed themselves to meet best-practice standards in price reporting, including with respect to staff training, supervision and methodology application. In addition, as discussed in more detail below, the IPRO Code requires compliance with IOSCO's PRA Principles in relation to all benchmark prices produced by an IPRO.

As Ofgem identifies quite correctly in section 2.22 and figure 4, there is an open and competitive marketplace of suppliers of price assessments and price references. There is strong competition not only between the number of PRAs active in the marketplace, but also from a wide range of other suppliers including major newswire services such as Reuters and Bloomberg, brokers, exchanges such as ICE and other private data-service providers. Competition in the sector means that should a customer come to lose confidence in a particular PRA or other supplier in the sector — for example through loss of confidence in a particular methodology, or in the operational standards or any other aspect of that supplier's services — the customer can choose to adopt prices from a competing supplier. Because of the competitive nature of the marketplace, switching between suppliers occurs regularly. The wide choice of entities providing reference prices and the fierce competition between them exerts strong pressure on the sector to produce reliable and robust assessments at reasonable cost.

Argus Media would also like to comment on sections 2.25-2.27 of the call for evidence, which discuss the regulatory framework in which PRAs operate. In this context, Ofgem is quite right to note that *"While PRAs self regulate, they are still subject to regulatory scrutiny."* Indeed we believe that the degree of regulatory scrutiny that the PRAs now operate under bears emphasising, as it is often not well appreciated, particularly by commentators and casual observers in the general press.

PRAs now operate under what is in effect a strong regime of public accountability and regulatory oversight. This includes:

- The IOSCO PRA Principles, for all benchmark prices¹² produced by PRAs.

¹² The PRA Principles refer to 'benchmarks' as *"price assessments that are referenced in derivatives contracts"*. The PRA Principles further state that *"Although the PRA principles were developed in the context of PRAs and oil derivatives markets, PRAs are encouraged to implement the principles more generally to any commodity derivatives contract that references a PRA assessed price without regard to the nature of the underlying."* (PRA Principles, page 7) Argus Media and other leading PRAs have fully accepted this and are implementing the PRA Principles for all their benchmark prices across all commodities, not just oil.

- A requirement, under the PRA Principles, for an independent external auditor to conduct an annual audit of the PRA's compliance with the PRA Principles. The results of this external audit are required to be made publicly available.¹³ Argus Media will complete its first such external audit in September 2013 with results to be published by January 2014.
- Use by market authorities (in this case deemed to be the regulated exchanges such as ICE, CME, etc) of their approval/review authority over listed derivatives contracts to only permit trading/clearing in contracts that reference a PRA price assessment that fully complies with the PRA Principles¹⁴.
- The IPRO Code — a robust voluntary industry code of conduct drawn up by Argus Media, ICIS and Platts, and now finalised. (Please see our response to question 5 for further discussion.) The scope of the IPRO Code extends to all price reporting activity by an IPRO. It requires annual public attestation of compliance with the Code as well as adherence to IOSCO's PRA Principles in relation to all benchmark prices produced by an IPRO.

IOSCO has referred to the IPRO Code as a "key work stream" on benchmark initiatives¹⁵. Martin Wheatley, Chief Executive of the Financial Conduct Authority (FCA) has acknowledged the IPRO Code's role, noting that *"Further, PRAs have agreed an industry code for Independent Price Reporting Organisations (IPROs), which covers best practice with respect to governance, conflicts of interest and transparency. These responses [the IPRO Code together with IOSCO's PRA Principles] may be sufficient to ensure credibility in the oil markets"*¹⁶. While, in the context of the time period of his comments, Martin Wheatley specifically referenced oil, the scopes of both the IPRO Code and IOSCO's PRA Principles have been confirmed to extend to all commodities.

- A framework of applicable legislation that includes REMIT and the updated MAD/MAR regime¹⁷ in Europe, which prohibit manipulation of a benchmark, as well as similar legislation either already in force or expected shortly to be so in other major international jurisdictions.

Taken together, these multiple and complementary elements constitute a strong regime of public accountability and regulatory oversight for the PRAs.

¹³ Principle 2.21 of the PRA Principles

¹⁴ *"Timely and effective mechanisms for implementing the principles should include the following... The use by a market authority of its rule approval and/or review authority over derivatives contracts, as appropriate, to refuse admission to exchange trading or central clearing of any derivatives contract that references a PRA-assessed price which, in the opinion of the market authority, has been developed under policies and procedures that do not reflect effective implementation of the PRA principles and call into question the reliability of an assessment."* (PRA Principles, page 8)

¹⁵ IOSCO CR01/13, p6; CR04/13, p3; FR07/13, p3

¹⁶ The Wheatley Review of LIBOR: Final Report, section 7.26 (page 58)

¹⁷ REMIT is in force. The revised MAD/MAR regime is currently passing through final stages of legislative scrutiny in the 'trialogue' process between the relevant EU institutions. In the meanwhile, the 2003 MAD directive (2003/6/EC) is in force. While this does not contain an explicit prohibition on manipulation of a benchmark, it includes prohibitions on the dissemination of false or misleading information through the media.

Question 2: What is your company's policy on providing information to price reporters or other benchmarking services?

This question is targeted at market sources, but it is also a question of central importance to the PRAs. Contributions by market sources in energy markets are entirely voluntary. Ofgem notes:

"...price reporting agencies rely on market participants to supply them with good quality information"¹⁸; and

"some participants have stated publicly that they do not provide information to PRAs."¹⁹

There is a clear public interest in encouraging market participants to contribute to overall market transparency by providing information to PRAs. In our experience, one factor in the hesitation and sometimes unwillingness of some market participants to supply price information to PRA journalists is their confusion about official attitudes and/or their perception that they place themselves at legal or financial risk by doing so. Understandably, the recent focus by Ofgem, DG COMPETITION and DG MARKT on possible manipulation by market sources has led market participants to question whether they should continue to provide information to PRA journalists. Some participants appear to believe that authorities would prefer them not to, while others consider the (avoidable) risks are not worth the taking. Some major market participants have stated publicly, or have been reported in the media to have confirmed, that they do not provide price information to PRAs or no longer do so.²⁰

As Ofgem perceptively notes:

"greater regulatory scrutiny of the information flows could introduce a perception of risk (irrespective of whether the risk is real) to those providing the information... the simplest way to mitigate this risk may be to withdraw cooperation and decline it. This in turn can lead to a breakdown in the quality of the price assessment process, with negative consequences for the market and for consumers."²¹

We would like sectoral regulators and competition authorities to keep in mind that regulatory interventions can unwittingly lead to market participants withdrawing their contributions to market transparency. For example, DG MARKT's draft EU regulation on benchmarks would place unlimited financial and legal liability on market sources as well as establishing detailed rules around how they should supply information. As already mentioned, MAR Article 8.1.d would punish honest mistakes by market sources. Measures such as these do nothing at all to encourage market participants to voluntarily contribute to market transparency. They "introduce a perception of risk" with the unintended negative consequences noted by Ofgem above.

There is a need for regulators to remodulate their messaging and to find ways that encourage, rather than discourage, contributions from market sources, thus supporting market transparency. Present messaging is unclear and too often negative. We would like to see Ofgem and ACER taking a

¹⁸ Ofgem call for evidence, Executive Summary, paragraph 1

¹⁹ Ofgem call for evidence, note 18

²⁰ www.centrica.com/index.asp?pageid=1041&newsid=2609
www.ft.com/cms/s/0/b96b6cbc-b7d9-11e2-9f1a-00144feabdc0.html#axzz2a9V3DlkU
www.reuters.com/article/2013/07/29/metals-libor-idUSL6N0FZ2AH20130729

²¹ Ofgem call for evidence, section 2.19

pro-active leadership role. The result should be greater transparency in wholesale energy markets, which in turn would support competition, new entrants to the markets and improved market liquidity.

Question 3: *In what ways do you use benchmarking prices by price reporting agencies or other price benchmarking services?*

This question is targeted at the users of PRAs and other price benchmarking services. It may though be worthwhile our highlighting that Argus Media's clients are spread across a wide spectrum of business, public sector, academic and other users. Argus Media publishes several thousand price assessments on a daily basis. There are no reliable data available — either publicly or privately — on how PRA price assessments are used (a point Ofgem notes in section 2.3). But based on our interactions with our customers and the feedback and our general understanding from them on how they use our products, the majority of our price assessments are used only for informational and ad-hoc analysis purposes. Only a relatively small percentage of our price assessments are used as price references of some kind (eg in long-term supply contracts). And only a very small minority have been adopted by clients for use as benchmarks to settle derivatives contracts.

Question 4: *Do you use a single provider only, or a combination or variety of prices?*

This question is targeted at the users of PRAs and other price benchmarking services. It may though be worthwhile rehighlighting the diversity of available suppliers — as Ofgem explains well in section 2.22 and figure 4 — and the strong competition in the sector. Our understanding, based on our interactions with our customers, is that among active market participants (who, as we noted earlier, form only a subset of our overall subscriber base), many subscribe to more than one provider.

Question 5: *What are your views on the terms of the IPRO code of conduct and the various methodologies of the price reporting services with particular reference to gas and electricity markets?*

While this question is targeted at market participants and other stakeholders, it may perhaps be helpful for us to provide some commentary on the IPRO Code that is now fully finalised.

The IPRO Code has recently been finalised by its developers, Argus Media, ICIS and Platts. It will come into effect from 1 September 2013. Argus Media became a signatory to the IPRO Code on 30 July 2013.

As discussed in Ofgem's call for evidence and as commented on earlier in our response, since the IPRO Code was first released in draft form in 2012 for stakeholder consultation, there have been multiple benchmark work streams in multiple jurisdictions. The developers of the IPRO Code wished to consider all these work streams in their own work to finalise the IPRO Code. These streams have included IOSCO's PRA Principles, IOSCO's broader work on financial benchmarks, work by the Institute of Chartered Accountants in England and Wales (ICAEW) on audit guidance for the PRA

Principles, the ESMA-EBA work stream on benchmarks, the UK review of Libor and associated domestic legislation, Singapore MAS' work on benchmarks and the European Commission's benchmark work stream.

This has, inevitably, made the finalisation process for the IPRO Code more lengthy and complex than ideal. Nevertheless this work has now been completed. The IPRO Code has been finalised both in light of the stakeholder feedback received during the public consultation period and also with regard to the numerous other work streams noted above. A suitable period of time has been allowed between finalisation of the IPRO Code and its coming into effect (1 September 2013) to enable other IPROs to consider signing the Code as an original signatory. After 1 September 2013 the IPRO Code will of course remain fully available to all IPROs to sign up to.

In drafting and finalising the IPRO Code, its developers were guided by a number of key principles, including:

- **Rigorous, voluntary, with “teeth”:** The Code should be a robust voluntary industry code of conduct, with real teeth, codifying a set of best-practice standards for independent price reporting organisations.
- **Application to all price reporting:** The Code should apply to the totality of an IPRO's price reporting activities, and across all commodities that the IPRO is active in reporting on.
- **Non-discriminatory:** The Code should be available to any independent price reporting organisation willing to adhere to its requirements.
- **Proportionate and pro-competitive:** The Code should be proportionate, bearing in mind the wide range of independent price reporting organisations in the market — from larger global operators active across many commodities to small regional or local organisations in single and highly specialised markets. It should be pro-competitive and while establishing best-practice standards it should not seek to reduce competition in or to foreclose new entrants from the IPRO marketplace.
- **Incorporates IOSCO's PRA Principles:** The Code should require compliance with IOSCO's PRA Principles for all applicable price assessments.

As noted in the final bullet above, the IPRO Code requires IPROs to comply both with IOSCO's PRA Principles for all applicable price assessments (see footnote 12 to our response) *and* with the IPRO Code.

While there are naturally many close similarities between the IPRO Code and IOSCO's PRA Principles, the two are not identical. In part this reflects their different provenances and histories — with work on the IPRO Code predating other benchmark work streams including IOSCO's work on the PRA Principles.

For example, the standards of good IPRO governance required under the IPRO Code are significantly more detailed than under the PRA Principles. In other areas, proportional application and consideration of the wide diversity of IPROs across a wide range of commodity markets have also resulted in differences.

The IPRO Code provides for robust monitoring of compliance — an IPRO’s most senior executive officer is required annually to make a written public attestation of the IPRO’s compliance with the Code or provide a written explanation of any material non-compliance and remedial action to rectify. Under the IPRO Code, those IPROs with obligations under the PRA Principles must in addition undergo external audit as required under the PRA Principles.

In considering differences between the IPRO Code and IOSCO’s PRA Principles, it is worth noting that much of the latter applies at an organisational level — such as the PRA governance and conflicts of interest requirements, training and supervision of market reporters (‘assessors’ in IOSCO’s terminology), engagement with stakeholders, complaints handling, etc. These requirements of the PRA Principles by nature can only be implemented across a PRA’s whole price reporting operations, rather than only applying to specific price assessments.

In contrast, other aspects of IOSCO’s PRA Principles are more granular and apply at the specific price assessment level. While again most of these requirements can be applied by IPROs across their complete price reporting operations, in a small number of cases it would not be practical or proportionate for IPROs to do so for each and every price assessment they publish. For example, Principle 2.3 of the PRA Principles would be disproportionate and simply impossible in practice for many IPROs to apply to every single price assessment. This point was discussed with IOSCO and recognised during the stakeholder engagement to develop the PRA Principles.

Ofgem is quite correct in noting that *“Although specific to oil (which has some unique characteristics as a commodity) many of the findings and recommendations from this work [IOSCO’s PRA Principles] are directly applicable to the reporting of gas and electricity prices.”*²² We would though emphasise that some aspects of the PRA Principles could not practically be implemented for every single price assessment published by a PRA. This is reflected in the IPRO Code, which has specifically been designed as best-practice standards to apply across the totality of an IPRO’s price assessment activities.

As noted in our response to question 3, the majority of Argus Media’s price assessments are used only for informational and ad-hoc analysis purposes, with only a relatively small percentage used as price references in some format and only a very small minority adopted by clients for use as benchmarks in derivatives contracts. In this sense IOSCO has wisely embedded proportionality into the PRA Principles in restricting their application to price assessments that the market uses as benchmark prices for settling derivatives. These are the most significant price assessments in terms of usage and relevance, since market participants only adopt for derivatives usage those price assessments that are widely used as a price reference of some kind (for example in price indexation of long-term supply contracts).

Question 5 also seeks comments in relation to PRA methodologies, particularly with respect to power and gas markets. Here we would note that all Argus Media methodologies are developed through extensive consultation with market participants — and this is a strong component of both the IPRO Code and the PRA Principles. Other requirements under both the IPRO Code and the PRA Principles include routine review of a methodology’s fitness for purpose and consultation with stakeholders over any proposed material change in a methodology.

²² Ofgem call for evidence, section 1.4

As Ofgem observes, “*Trades may take place at different values, depending on what individual buyers are willing to pay and individual sellers are willing to accept and hence there is no single “price” for over the counter trades, but many different prices. As such there is demand for services which can generate prices that represent a fair value of trade in the market.*”²³ Thus, in practice, it is neither practical, nor likely, for a PRA to achieve 100% consensus among market participants in regard to a particular methodology or proposed change, partly given market participants’ own natural positions in the market.

As Ofgem identifies in section 2.22 and figure 4 of the call for evidence, and as we discuss in our response to question 1, there is an open and competitive marketplace of suppliers of price assessments and references. This means that market participants can choose from a range of suppliers and a range of methodologies; or indeed they can decline to use any service at all.

Question 6: *In the context of GB gas and electricity markets, do you consider the current arrangements whereby price reporting agencies operate under a self-regulatory regime are fit for purpose?*

Argus Media would make four points in response to this question.

1. The IPRO Code is now finalised and will come into effect from 1 September 2013. It applies to all price assessments.

The now finalised IPRO Code applies to all price assessments produced by an IPRO. It is a robust industry code of conduct to demonstrate and ensure that all IPRO signatories meet best-practice standards across their entire price reporting activities. It provides enhanced public accountability through public attestations of compliance. It also requires any IPRO with obligations under IOSCO’s PRA Principles to comply both with the PRA Principles and with the IPRO Code.

While many of the PRA Principles themselves are applicable across all of a PRA’s price reporting activities (particularly the aspects on good governance, conflicts of interest management, market reporter training and supervision, record keeping, engagement with stakeholders, complaints handling), some aspects of the PRA Principles would be disproportionate and could not practically be implemented for every single price assessment published by a PRA. In contrast, the IPRO Code applies to all price assessments published by an IPRO.

2. The PRAs are extending the PRA Principles to all price assessments used as benchmarks, and not just to oil benchmarks.

IOSCO’s PRA Principles state:

“Although the PRA Principles were developed in the context of PRAs and oil derivatives markets, PRAs are encouraged to implement the principles more generally to any

²³ Ofgem call for evidence, section 2.13

*commodities derivatives contract that references a PRA assessed price without regard to the nature of the underlying.*²⁴

This sentence was repeated by IOSCO Committee 7 in March when it published a synopsis of the PRA benchmark work stream as part of an Implementation Questionnaire it sent to the PRAs.

As a result of this explicit IOSCO encouragement, the PRAs are extending the application of the PRA Principles to all their benchmarks, and not just to oil benchmarks.

3. The self-regulatory regime includes clear public accountability through the IPRO Code. For PRAs with obligations under the IOSCO PRA Principles, this is further buttressed by two independent validation mechanisms, one of which provides direct regulatory oversight by market authorities.

- IPRO Code: Includes formal public attestation, on an annual basis, of compliance or explanation of non-compliance and of remedial actions to address
- PRA Principles: Annual external audit (Principle 2.21)

Requirement for an independent external auditor to conduct an annual audit of the PRA's compliance with the PRA Principles, with results of the audit to be published. The Institute of Chartered Accountants in England and Wales (ICAEW) is currently finalising guidance to assist external auditors that perform assurance audits on the PRA Principles.

- PRA Principles: Oversight by market authorities

In its Final Report on the PRA Principles, IOSCO recommends *"The use by a market authority of its rule approval and/or review authority over derivatives contracts, as appropriate, to refuse admission to exchange trading or central clearing of any oil derivatives contract that references a PRA-assessed price which, in the opinion of the market authority, has been developed under policies and procedures that do not reflect effective implementation of the PRA Principles and call into question the reliability of an assessment."*²⁵

The last two bullets provide strong independent assurance mechanisms that the regime recommended by IOSCO for PRA benchmarks will be fit for purpose. However, we should in fairness point out that this is "work in progress". The IOSCO 18-month period for implementation and evaluation has yet to fully run its course.

4. Price reporting operates under a framework of applicable legislation that includes REMIT and the updated MAD/MAR regime in Europe, which prohibit manipulation of a benchmark, as well as similar legislation in other major international jurisdictions.

²⁴ IOSCO PRA Principles, page 7

²⁵ IOSCO PRA Principles, page 8

Question 7: Are there any other issues that you wish to raise in the context of this call for evidence?

We would like to comment on potential “next steps”, which are referred to in several passages of the Ofgem paper and include facilitation to support effective self-regulation through to a more significant intervention.

As already suggested in our response to question 2, we would like to see Ofgem and ACER play a more pro-active role in encouraging market participants to supply information to PRA journalists. This could take various forms, such as open letters to industry, and positive statements from senior regulators at industry conferences and to the general media. As just one possible practical next step, Argus Media would be pleased to participate in a stakeholder roundtable under Ofgem auspices to discuss with market participants practical measures to help achieve full provision of data to PRAs.

Beyond this, we would also encourage Ofgem and ACER to assist DG MARKT to understand the differences between financial and commodity markets and how the distinctive benchmarking processes in energy markets respond to the characteristics of those markets.

We also feel a need to place on record the journalistic basis of Argus Media’s activities, which Ofgem itself refers to in section 2.15. This is one of the key differentiators with other types of benchmark activities, and one of its strengths. PRAs such as Argus Media are independent of the market and not inherently conflicted. PRAs are not market participants and, consequently, they have no vested interest in the level of any price that they publish. Instead, and as Ofgem points out, PRAs “*have a strong commercial incentive to ensure that their customers retain confidence in their products.*”²⁶

Journalists employed by Argus Media produce price assessments, and not benchmarks *per se*. It is the market itself that decides whether to use any assessment as a benchmark, and only a small fraction of the many thousands of price assessments that are produced each day by Argus Media journalists are used as benchmarks. To be clear, in the case of Argus Media there is no activity of “benchmark setting” that is separate from the journalistic activity of providing assessments and market commentary that underpins those assessments. The small fraction of Argus Media assessments that the markets themselves decide to use as benchmarks are produced in precisely the same journalistic way as the great majority of price assessments that are not used as benchmarks.

The reason for drawing attention to the journalistic foundation of Argus Media’s activities is not just to point to its strengths, when compared with Libor and similar conflicted benchmarking processes, but also as a reminder that there are no precedents in the UK for regulation of the media. The closest analogy we are aware of is *The Investment Recommendation (Media) Regulations 2005* which are available at

http://ec.europa.eu/internal_market/finances/docs/actionplan/transposition/uk/d13.4-ml-2-uk.pdf.

HM Treasury’s Explanatory Note at the back of the regulations is clear and informative. This initiative was to reinforce, rather than replace, media self-regulation.

²⁶ Ofgem call for evidence, section 2.23

I hope that our responses are helpful. Please do not hesitate to contact me in the event of any queries or if we can provide any further clarifications. Argus Media continues to offer its assistance to Ofgem as it progresses its analysis and considerations; we welcome further engagement.

Yours sincerely,

Simon Smith

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