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30 August 2013

Dear Graham

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

Thank you for providing SSE with the opportunity to provide its views on the current pricing benchmark arrangements for the gas and electricity markets. We have provided our detailed response to the questions posed in the call for evidence in the attached annex.

SSE agrees that good quality price benchmarks are a key component of an effective functioning market. Price benchmarks can be used in a range of ways by both market participants and other industry stakeholders. Given the extent to which they are used in contracts and financial instruments it is important that all stakeholders have confidence in their integrity, as ultimately the costs incurred by market participants may be passed on to customers.

As Ofgem points out, recently there has been increased regulatory scrutiny of how prices are formed and benchmarked in a variety of markets, including the gas and electricity markets, and this has been widely reported in the press. It therefore seems appropriate that Ofgem takes the opportunity to consider the position of current arrangements in the gas and electricity markets and whether they are fit for purpose. Following completion of this review, it is critical for the effective operation of these wholesale markets that Ofgem is able to publicly state that it has confidence in them.

As Ofgem would expect, as an active participant in the gas and electricity markets (as well as other linked markets such as coal and oil), SSE uses price benchmarking agencies.

For example:

- we use Price Reporting Agency (PRA) assessments of forward prices in our risk management processes;
- these forward prices inform our forecasts of the likely future running of thermal plant - and therefore inform our fuel buying requirements;

- this dependence on PRAs demonstrates our level of confidence in the reported market assessments; and
- our long term contracts may also incorporate PRA reference prices in price indexation.

Whilst welcoming Ofgem's review, SSE would strongly caution against intervention on PRAs that could undermine market confidence in the process - or in a way which may dissuade market participants from reporting trading activity. We note that the business models of Price Reporting Agencies such as Heren, Argus, and Platts depend critically on market trust in the quality of the data. In addition, the advent of REMIT ensures that market participants can have confidence that allegations of market manipulation will be taken seriously and investigated appropriately.

I hope that the foregoing and the attached are a useful contribution to the call for evidence. Should you wish to discuss any of the above, please do not hesitate to contact me on the above number or Roger Hutcheon on 01738 456726.

Yours sincerely



Katherine Marshall
Head of Regulation, Markets

Ofgem call for evidence on price benchmarks and price reporting agencies

Detailed response to consultation questions

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

We agree with Ofgem's assessment of the issues for the reasons set out in our cover letter.

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

SSE's Energy Portfolio Management department has a formal policy in place covering this. In summary, prices will only be provided to external parties who have a genuine market facilitation role requiring such information or have a commercial relationship with SSE Energy Supply Limited (SSE ESL) – the legal entity under which wholesale energy trading activities are undertaken. This would include, for example, exchanges and market report providers and customers and their consultants. Currently only one Price Reporting Agency (PRA) – Heren and four brokers (Tullett Prebon, Intercontinental, Spectron and Platts) are on the approved list.

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

There are a wide variety of contracts and trade types (external and internal, derivatives and physical, differing commodities) that SSE ESL is a party to that reference benchmark prices.

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

We use a combination. Heren and Argus are the most commonly referenced PRAs in SSE ESL's dealings.

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

The codes of conduct applied by Argus, Heren and Platts are inconsistent. On paper, Platts' Code is the most comprehensive and Argus's the least, although each firm has significant "holes" in key areas. We consider that all firms should be required to have clear requirements as a minimum with regard to confidentiality, misleading behaviour, improper disclosure, bribery, gifts and hospitality, misuse of information, fraudulent practices, conflicts of interest and misuse of third party information. In addition, PRAs should have stated policies on requirements for staff (for example, with regard to integrity and responsibility).

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?

Yes. We believe that there is significantly more downside risk (i.e. a breakdown in the quality of the price assessment process) than potential upside benefit in trying to introduce formal regulation. Section 2.19 of

Ofgem's call for evidence provides a good analysis of this issue. There may, however, be a case for a hybrid solution that could introduce a registration and approval process and imposes a minimum required code of conduct for the industry (as articulated in our response to question 5 above) although we appreciate that it may be difficult to make this work in practice.

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

Robust price benchmarks are essential for market efficiency. We strongly believe that any regulatory intervention would result in a deterioration in the quality of those benchmarks, and in turn their credibility. This would have unintended consequences for the market overall, and would ultimately impact on customers.

We also believe that it is critical for the wholesale markets that Ofgem is able to publicly state that it has confidence in them on completion of this review.