



Making a positive difference
for energy consumers

To all wholesale market participants and
other interested parties

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Dear Colleagues,

Scarcity pricing and conduct in the wholesale energy market

The purpose of this letter is to set out Ofgem's position on the interaction between the pricing of scarcity in the wholesale energy markets and potential market conduct issues. In addition, we remind industry stakeholders of the importance of adhering to their legal obligations. This is as a result of concerns that have been raised with us in respect of certain behaviours that may be taking place within the market. For the avoidance of doubt, this letter is separate to any actions we may be considering in respect of individual market participants.

The price of a product will, among other things, reflect its scarcity. In the wholesale energy market we expect that in certain situations, for example where the margin between available capacity and peak demand becomes tight, a scarcity premium will be built into prices, and prices will rise accordingly. This price rise will provide a signal to the market that should encourage investment in production or a demand side response, which will be to the benefit of future energy consumers.

The market has in place a legal framework which governs behaviours to ensure the price setting mechanism can work correctly. This includes licence requirements, a number of industry agreements such as codes and the Regulation on Energy Market Integrity and Transparency (REMIT)¹.

REMIT's purpose is to safeguard the wholesale market's integrity through prohibitions on market manipulation and insider trading, and requires transparency of price sensitive information to ensure that prices are reflective of all significant information. To support the market participants' understanding of REMIT, Ofgem has issued guidance on inside information disclosure² (in particular timely disclosure and the proper use of exemptions³) and developed examples on what might constitute market manipulation⁴. We have stated our support for the guidance⁵ the Agency for the Cooperation of Energy Regulators (ACER) has published regarding the application of REMIT prohibitions and obligations and have

¹ Regulation (EU) No 1227/2011 of the European Parliament and of the Council of 25 October 2011 on wholesale energy market integrity and transparency.

² https://www.ofgem.gov.uk/sites/default/files/docs/2014/07/ofgem_open_letter_on_remit_inside_information_0.pdf

³ When market participants decide to use the exemptions available under Articles 3(4)(b) or 4(2), they must use the following link to properly notify Ofgem and ACER: <https://www.acer-remit.eu/np/home>.

⁴ https://www.ofgem.gov.uk/sites/default/files/docs/2015/09/20150814_remit_open_letter_september_2015_0.pdf

⁵ https://www.acer-remit.eu/portal/custom-category/remit_guidance_and_recommendations

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recommended market participants take this into account along with guidance we have issued ourselves⁶.

In addition to REMIT, market participants must comply with the requirements of (amongst other things) both the Grid Code and Balancing and Settlement Code (BSC) in so far as applicable to them. In particular, plants should ensure that the technical parameters they submit to the System Operator represent their best estimates and are prepared in line with Good Industry Practice. The Grid Code defines Physical Notification as "data that describes the BM Participant's best estimate of the expected input or output of Active Power of a BM Unit and/or (where relevant) Generating Unit, the accuracy of the Physical Notification being commensurate with Good Industry Practice". Good Industry Practice is defined as "the exercise of that degree of skill, diligence, prudence and foresight which would reasonably and ordinarily be expected from a skilled and experienced operator engaged in the same type of undertaking under the same or similar circumstances".

Submitting misleading Physical Notifications or other physical parameters clearly has the potential to breach one or more of these obligations. Ofgem takes its responsibilities with respect to market conduct very seriously and monitors the market to probe potential breaches. Where we become aware of breaches we have powers under REMIT and other statutory provisions to ensure compliance. Under REMIT we may publicly censure, place unlimited financial penalties or institute criminal prosecutions.

We note that REMIT and other rules on market conduct are not intended to interfere with the proper application of market forces, nor do they prohibit a rise in market prices reflective of scarcity in the market. Where there is no evidence of market abuse and price rises are reflective of scarcity, we would not expect REMIT or other market conduct processes to be engaged.

If you have any specific questions regarding REMIT or market conduct please email REMIT@ofgem.gov.uk. If you would like to report any specific market conduct concerns, please email Market.Conduct@ofgem.gov.uk.

Yours sincerely,



Cathryn Scott
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⁶ This includes Ofgem's REMIT procedural guidance:
https://www.ofgem.gov.uk/system/files/docs/2016/09/remit_procedural_guidelines.pdf