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Cathryn Scott
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20 September 2018

Dear Cathryn,

**Proposed suspension of the MMO licence condition pending further review**

We are writing in response to Ofgem's open letter of 9 August proposing to suspend the Market Making Obligation (MMO) pending further review. As one of the parties still subject to Schedule B of Special Condition AA of the Generation Licence (the MMO), we welcome the opportunity to provide views on the courses of action outlined in the letter.

Following Ofgem's directions to release E.ON and now Centrica from the MMO, it will fall to the four remaining obligated parties to absorb MMO trading volumes previously undertaken by these companies. Our MMO trading volume in 2017 was [✄]TWh, more than twice the combined trading volume for our Retail, Renewable and Generation businesses ([✄]TWh), which exposed us to significant cost and credit risk. If Ofgem were to retain the obligation, we would be faced with an even higher level of credit and cost risk, which we consider would be entirely disproportionate.

Indeed, since Centrica was removed from the obligation on 9 August 2018, the four remaining obligated parties have already been exposed to a significant increase in risk and costs due to market volatility driven largely by:

- EU carbon allowances (EUAs) rallying from €17.50/te to €25.23/te before declining back down to €18/te;
- National Balancing Point (NBP) gas prices rallying strongly, with winter 18 rising from 65 p/th to 82p/th before declining to 74p/th;
- UK generation switching from gas to coal in the winter 18 period, which further increased power market volatility.

During this same period, the monthly average volume we traded in the market making window increased 100%[1] and year to date costs increased by around 62%[2] due to the increased volatility now having to be managed by four parties rather than six. This volatility shows no signs of easing in the coming weeks and may well increase further as we approach the winter period.

[1] Relative to the monthly average traded in the previous 7 months.
[2] Year to date costs in early August 2018 compared to year to date costs at 14 September 2018.

Given that two of our larger competitors in the supply market are now exempt from the obligation, we consider that retaining it for ScottishPower would be discriminatory. Moreover, as Ofgem notes, upcoming changes in the market may further reduce the number of obligated parties, rendering the obligation on the few remaining parties even more disproportionate and discriminatory.

Therefore, we fully support Ofgem's minded to position to suspend the MMO until the review is completed in 2019, and we request that a direction is issued alongside a decision on this consultation which suspends the MMO with immediate effect. This should be done as soon as possible to limit the exposure of remaining obligated parties to costs and risks from peaks in winter trading, and ideally before the transition to PAR1 on 1 November.

Should Ofgem decide to suspend the MMO, we assume there would be a corresponding suspension of relevant reporting requirements with effect from the date that the MMO ceases.

We believe that without the MMO in operation, market participants can remain confident of fair market access and robust reference pricing for the following reasons:

- the SMA obligation will remain in place, guaranteeing market access on fair terms to Eligible Suppliers;
- Price Reporting Agencies will continue to independently report the forward curve on a daily basis and brokers and exchanges will continue to operate market places with live trade orders and recent trade prices made available to all subscribers;
- any perceived risk of inappropriate behaviour by larger market participants has diminished with the implementation of the Regulation on Wholesale Energy Market Integrity and Transparency (REMIT); and
- the GB wholesale market today is much less characterised by vertically integrated business models, resulting in an increased contribution to market liquidity from multiple market participants.

We have previously encouraged Ofgem to consider a competitively appointed market maker as an alternative to the MMO, and we continue to believe this could be worth exploring. We suggest that Ofgem monitors the impact of the suspension on market liquidity and assesses whether there might be a case for such an intervention after, say, a year.

Finally, we also agree with Ofgem's minded to position not to proceed with a statutory consultation on changes proposed in the policy consultation that concluded on 7 February 2018. Business models and market arrangements have evolved considerably since that consultation and it is a pragmatic move to consider those proposals within the scope of the 2019 review.

Should you wish to discuss any of these points further, please do not hesitate to contact me.

Yours sincerely,

Richard Sweet

**Richard Sweet**
Head of Regulatory Policy