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Dear Heather

Open Letter: Secure and Promote Update

We welcome and fully support Ofgem's minded to decision to suspend the Market Making Obligation licence condition (Schedule B of Special Condition AA of the Generation Licence) until a further in-depth review of this provision is completed.

We have long been advocating for a fundamental review of the Market Making Obligation (MMO) given that the market has fundamentally changed since the intervention took effect in March 2014. While this fundamental review is still pending but only four obligated parties are now remaining, it is our view that Ofgem's minded-to decision to introduce a suspension is a prudent step to ensure that the remaining licensees do not face disproportionate costs and risks while delivering the obligation.

Based on Ofgem's estimates[1] in 2013, ongoing costs of the MMO intervention were assessed between £969k and £4.8m a year per licensee, reflecting 'low case', 'best estimate' and 'high case' scenarios, excluding the costs associated with reporting requirements. Given that two out of six initially obligated parties are now exempt from delivering the obligation, it is reasonable to expect that the costs incurred by the remaining licensees will increase as a result of the proportionally larger volumes traded through these parties. Furthermore, it might become increasingly difficult for the licensees to manage the size of the positions opened as a result of the MMO and the associated costs of these positions. In a volatile market the costs of the MMO are likely to be above the cost range estimated by Ofgem in 2013. We also consider that an increased pressure on the obligated licensees to process a

[1] https://www.ofgem.gov.uk/ofgem-publications/84511/impactassessment-wholesalepowermarketliquidity-statutoryconsultationonthesecureandpromotelicencecondition-pdf

higher volume of trades might also impact a compliant delivery of this obligation and result in increased reputational risks and financial penalties for the parties.

We do not consider that the existing parameters of the MMO, such as a net volume cap of 30MW, allow to mitigate the above-mentioned risks. For example, our experience has been that we can trade well over 30MW for a front month in any one window where this month overlaps with the front quarter and front season products. In cases where we are 'lifted'/'hit' on all three products, our exposure could be up to 180MW short/long in a front month peak product.

We are supportive of the full suspension of the MMO as soon as possible, preferably by the start of the winter season but no later than by 1st November 2018, when PAR1 is to come into effect. This will ensure that the remaining obligated parties are not being hit by disproportionate costs and risks of delivering the MMO during the period when price volatility is expected to increase.

Separately, it is our view that the fundamental review of the MMO, which Ofgem intends to conduct over 2019, must reassess a rationale for and the benefits of market making in the wholesale energy market. Where unambiguous evidence suggests that market making continues to be necessary, we support Ofgem's proposal to review the MMO criteria, parameters of this obligation as well as alternative delivery mechanisms for market making.

Kind regards

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