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30 September 2014

Energy Markets and Consumers Team
Department of Energy & Climate Change,
4th Floor Area C,
3 Whitehall Place,
London, SW1A 2AW

Via Email: arvin.jeboo@decc.gsi.gov.uk

Consultation reference: URN 14D/277

Re: Consultation on strengthening the regulation of wholesale energy markets through new criminal offences

Dear Sirs,

The Global Financial Markets Association (GFMA)¹ is pleased to provide responses to the Department of Energy and Climate Change's Consultation on strengthening the regulation of wholesale energy markets through new criminal offences.

Our responses to the questions raised by the Consultation are set out in Annex 1 to this letter. However, by way of a summary we would like to flag the following points in particular:

- We strongly agree that there is no case for criminalizing breaches of Articles 4, 8, 9 and 15 REMIT;
- We agree that it is necessary to clarify the territorial scope of REMIT, and that in the absence of clarification from the European Commission any UK criminal regime should have a clearly defined territorial scope;
- We agree that it is appropriate to adopt an approach requiring a person to have intended to commit an offence or to have been reckless as to whether an offence was committed. We would welcome further clarification of the mental element to the offences of insider dealing and market manipulation;

¹The Global Financial Markets Association (GFMA) brings together three of the world's leading financial trade associations to address the increasingly important global regulatory agenda and to promote coordinated advocacy efforts. The Association for Financial Markets in Europe (AFME) in London and Brussels, the Asia Securities Industry & Financial Markets Association (ASIFMA) in Hong Kong and the Securities Industry and Financial Markets Association (SIFMA) in New York and Washington are, respectively, the European, Asian and North American members of GFMA. For more information, please visit <http://www.gfma.org>.

- We consider that the proposed criminal regime should include appropriate defences or safe harbours in relation to insider dealing and market manipulation, based on the defences and safe harbours available in relation to the securities market abuse regime.

GFMA appreciates the opportunity to provide comments on the Consultation and would be happy to discuss our response with you.

Sincerely

A handwritten signature in black ink, appearing to read "David Strongin". The signature is fluid and cursive, with a prominent initial "D" and a long, sweeping horizontal stroke at the end.

David Strongin
Executive Director, GFMA

Annex 1

Q1. Do you know of any evidence about or examples of energy market manipulation or insider trading practices that should be taken into account in decisions about the proposed offences?

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Q2. Do you think that the territorial reach of the regulators' functions in respect of REMIT enforcement should be clarified?

Yes, we strongly agree that the territorial reach of the regulators' functions in respect of REMIT enforcement should be clarified.

It would be useful if the European Commission could clarify a number of points regarding the territorial scope of REMIT, including:

- The meaning of "any market within the Union" in the context of the definition of "wholesale energy market". This is important for determining whether or not a person is a "market participant" as defined in REMIT, but is not clearly defined. The Commission's proposed Implementing Act under REMIT refers to "organized market places", which as defined to give more detail on the types of markets that would be within scope, but the definition does not appear to have any defined territorial scope and appears to cover any market anywhere in the world that meets the definition.
- The scope of the enforcement powers of regulators in each Member State in relation to breach of obligations under REMIT, in particular to clarify whether a market participant may be subject to sanctions in more than one Member State in relation to the same behavior.

In the absence of any clarification from the European Commission on territorial scope of REMIT, it will be important that any UK criminal sanctions set out clearly the territorial scope of the UK criminal regime.

We welcome the statements in paragraphs 3.10 and 4.5 of the Consultation that the proposed criminal regime should focus on activities with a "clear UK element". However, while the indicators for what would constitute a "clear UK element" as set out in the Consultation are a useful starting point, we would welcome clarification on the following points:

- Paragraph 3.13 of the Consultation states that the proposed criminal regime would cover "acquiring or disposing of a REMIT product where the defendant (which could be any party to the trade) is in the UK".

- The proposed criminal regime should clarify what is meant by "any party to the trade". For example, does this mean any party to the trade who is a "market participant" as defined in REMIT? It is currently unclear exactly who would qualify as a "market participant" under REMIT (e.g., does this include persons who enter into transactions as agent rather than as principal, or clearing members who accept a trade for clearing after execution).
- The proposed criminal regime should also clarify what is meant by "in the UK". The Criminal Justice Act 1993 states that an individual must have been within the United Kingdom at the time when he is alleged to have carried out the relevant conduct. To the extent that the proposed criminal regime for breaches of REMIT applies to individuals, it may be appropriate to reflect the wording of section 62 of the Criminal Justice Act regarding territorial scope of the insider dealing regime. To the extent that the proposed criminal regime applies to legal entities, it will need to clarify what is meant by "in the UK" (e.g., where an entity has a branch, rep office or other place of business in the UK; where the relevant conduct was carried out by an employee of a branch in the UK; where the relevant conduct was carried out by an employee of the legal entity who happened to be within the UK at the time).
- Paragraph 3.13 of the Consultation also indicates that conduct may fall within the proposed criminal regime if "the transaction takes place in the UK (for instance, on a trading platform based in the UK or is subject to a jurisdiction clause in favour of a UK jurisdiction)".
 - The proposed criminal regime should clarify what is meant by a "trading platform" based in the UK. For example, does this mean a "wholesale energy market" as defined in REMIT, or an "organised market place" as defined in the Commission's proposed Implementing Act under REMIT? Both of these definitions raise questions as to the exact scope intended. Or would the proposed criminal regime provide a separate definition of "trading platform"? If so, it would be useful to understand what this definition would cover and whether there is any intention for Ofgem to publish a list of platforms which meet this definition.
 - The proposal to extend the criminal regime to transactions which are subject to a jurisdiction clause in favour of a UK jurisdiction could potentially cover a large number of contracts entered into by counterparties in jurisdictions outside the UK or EU, as jurisdiction clauses referring to the English courts or London Court of International Arbitration are commonly used around the world.

Q3. Do you agree that we should create criminal offences for the REMIT prohibitions on insider dealing and market manipulation?

We agree that there is a case for introducing criminal sanctions for breach of the REMIT prohibitions on insider dealing and market manipulation.

However, as discussed in our responses to the other questions in this Consultation, there are still significant aspects of the REMIT regime which are currently unclear (for example, in relation to the entities and products within scope as well as in relation to territorial scope). As a result, it may be appropriate to consider further whether it is proportionate to introduce criminal sanctions before these points of uncertainty have been addressed or before there has been an opportunity to examine these issues in light of the civil enforcement regime.

If it is considered to be proportionate to introduce criminal sanctions at this stage, the UK criminal regime will need to address these points of uncertainty.

Q4. Do you agree that the civil enforcement regime that is being created provides an effective deterrence to breaches of the REMIT requirements listed in the 2013 Regulations – including those around registration and the provision of information?

We agree that the civil enforcement regime provides an effective deterrent to breaches of the REMIT requirements listed in the 2013 Regulations. We strongly agree that there is no case for criminalizing breaches of Articles 4, 8, 9 and 15 REMIT.

Q5. Do you agree that an offence of insider dealing in wholesale energy products should be framed in this way?

We broadly agree with the way that the offence of insider dealing is outlined in the Consultation. However, we would welcome clarification on the following points:

- It would be useful to understand the extent to which guidance or case law in the context of securities market abuse would be taken into consideration in relation to the proposed offence of insider dealing. For example, there is a significant body of UK and EU case law around the question of when information would "be likely to significantly affect prices if made public".
- We agree with the proposal to adopt an approach requiring a mental element (i.e., whether a person intended to, or was reckless as to committing the relevant offence). The final regime will need to clarify which behaviour needs to be intentional in order to fulfil the mental requirement. For example, will it be sufficient for a person to deal intentionally while in possession of inside information (whether or not they know that they are in possession of inside information, and whether or not the inside information has contributed to the decision to deal), or

will it be necessary for the person to deal knowing that they are dealing on the basis of inside information? There has been a great deal of discussion regarding intent in relation to the securities market abuse regime, and it would be useful for this to be taken into account in framing the wholesale energy market abuse regime.

- The Consultation appears to indicate that there is a proposal to introduce a criminal offence of dissemination of price sensitive information. It should be made clear that the prohibited behaviour is not simply dissemination, but rather "dissemination other than in the normal course of the exercise of their employment, profession or duties", in line with REMIT and the securities market abuse regime.
- The Consultation indicates that the "most serious breaches" of REMIT should be punishable under the criminal regime. It would be useful to clarify what would be considered to be the "most serious breaches", and whether any breach with an element of intent or recklessness would be considered to be a "serious breach" for these purposes or whether there are additional criteria that would be considered.
- We have raised our questions in relation to the territorial scope of the insider dealing regime in our response to question 2 above.
- It will be important for a criminal regime to allow for appropriate defences. We discuss this further in our response to question 6 below.

We understand that the proposed criminal regime will not cover attempt to commit the relevant offences, so we do not discuss this further.

Q6. Do you consider that the exemptions set out above and in Chapter 4 are appropriate?

The exemptions set out in the Consultation reflect the exemptions set out in Article 3 REMIT. However, the proposed criminal regime should also include appropriate defences to avoid imposing a disproportionate burden on market participants.

The proposed criminal regime should provide for defences similar to those under section 53 and Schedule 1 to the Criminal Justice Act, and under the Financial Services and Markets Act 2000 (**FSMA**) and the Market Abuse Directive. For example:

- the defendant did not expect to make a profit as a result of the fact that the information was inside information;
- there was equality of information between the parties to the transaction;
- the defendant would have dealt anyway even if he had not had access to the inside information;
- the defendant was acting in good faith as a market maker;
- the defendant had in place effective information barriers (Chinese walls);

- the defendant was dealing to fulfil client orders and is carrying out those orders legitimately in the normal course of the exercise of their employment, profession or duties;
- the inside information in question arises solely as a result of the defendant's knowledge of their own intention to deal;
- research and estimates based on publicly available data should not be considered to constitute inside information;
- where a legal person has taken all reasonable measures to prevent market abuse from occurring, but nevertheless natural persons within their employment commit market abuse on behalf of the legal person, this should not be considered to constitute market abuse by the legal person.

If the proposed regime applies to both legal persons and natural persons, it will be necessary to consider appropriate defences for both legal persons and natural persons.

While these defences are not set out in REMIT, we consider that it should still be possible to provide for appropriate defences from the criminal regime so long as breaches of REMIT are also punishable under a civil regime. If DECC considers that it is not possible for the UK to introduce appropriate defences from the criminal regime, it should consider further whether it is proportionate to impose a criminal regime.

Q7. Do you agree that an offence of insider dealing should include legal persons and decision-makers?

We do not have any particular views on whether or not an offence of insider dealing should include both legal persons and decision-makers. However, any regime which applies to both legal persons and natural persons will need to define appropriately the behaviour which would constitute an offence for a legal person and for a natural person (and the circumstances, if any, in which an offence by a natural person would also constitute an offence by a legal person who employs that natural person) as well as appropriate defences or safe harbours for both legal persons and natural persons.

To the extent that the proposed regime is based on existing UK legislation (e.g., the Criminal Justice Act or FSMA), it should take into account the scope of that existing UK legislation and make appropriate amendments. For example, the Criminal Justice Act only criminalises behaviour by natural persons, so some of the behaviours or defences set out in that Act may need to be amended to reflect the scope of the proposed criminal regime.

Q8. Do you agree that the offence of energy market manipulation should be framed in the way described here?

We have similar comments on the proposed market manipulation regime to those raised in relation to the insider dealing regime regarding territorial scope, appropriate defences, what would constitute "most serious breaches" and the extent to which existing guidance and case law on the securities market abuse regime will be taken into account in framing the proposed wholesale energy market abuse regime. These are discussed in our response to question 5 above.

As with the proposed insider dealing regime, we agree with the proposal to adopt an approach requiring a mental element (i.e., whether a person intended to, or was reckless as to committing the relevant offence). As discussed above, the final regime will need to clarify which behaviour needs to be intentional in order to fulfil the mental requirement. For example, would it be sufficient for a person intentionally to enter into a transaction which has the effect of giving a false or misleading signal (even if the person did not intend or was not reckless as to that result), or would that person need to enter into a transaction intending to give a false or misleading signal.

Q9. Would the creation of these criminal sanctions change the processes that market participants are already putting in place to meet the requirements of the REMIT civil regime?

GFMA members do not expect to make significant amendments to their processes for compliance with REMIT as a result of the introduction of criminal sanctions. However, it may be necessary for market participants to put in place additional procedures to ensure compliance with any additional requirements imposed under the criminal regime (for example, introducing procedures and monitoring compliance with any safe harbours under the criminal regime).

Q10. Would the creation of these criminal sanctions change the level of confidence that market participants have in the fairness of the wholesale energy market?

In order to ensure that market participants have confidence in the fairness of the wholesale energy market, the proposed criminal regime would need to be clear regarding its scope and any available defences. If the proposed regime is not clear, this is likely to detract from the level of confidence that market participants have in the fairness of the market.