



Department
of Energy &
Climate Change

Strengthening the regulation of wholesale energy markets through new criminal offences

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Foreword

Our liberalised energy markets, which are underpinned by robust independent regulation, are a critical part of the UK economy. Effective competition in the wholesale energy markets is a key driver of lower prices which is why this Government is continuing to take steps to strengthen competition, so that markets work more effectively for consumers. I am committed to maintaining a strong and stable regulatory framework that delivers transparent and competitive markets and has the right penalties for those who step out of line. One component of this is having strong sanctions against those who abuse energy markets.

The wholesale energy market regulators have powers to deal with market manipulation and insider dealing in wholesale gas and electricity including the ability to impose unlimited fines, access to information and the power to enter premises. This consultation document sets out the case for new criminal offences of insider dealing in and the manipulation of wholesale energy markets. I am minded to create these new criminal offences so that energy markets and the consumers that rely on them have similar safeguards to those in place in financial markets in which the regulator has the ability to prosecute for criminal offences.

The Rt. Hon Edward Davey MP

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General information

Purpose of this consultation

This consultation seeks views on proposals to create new criminal offences of energy market manipulation and insider trading in energy markets.

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6 August 2014

Respond by:

30 September 2014

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Consultation reference: URN 14D/277

Territorial extent:

The United Kingdom.

References in this document to “the regulator” are to Ofgem in Great Britain and to the Northern Ireland Authority for Utility Regulation in Northern Ireland.

How to respond:

Your response will be most useful if it is framed as a direct response to the questions posed, though further comments and evidence are also welcome.

Additional copies:

You may make copies of this document without seeking permission. An electronic version can be found at <https://www.gov.uk/government/consultations/strengthening-the-regulation-of-wholesale-energy-markets-through-new-criminal-offences>

Other versions of the document in Braille, large print or audio-cassette are available on request. Please contact us under the above details to request alternative versions.

Confidentiality and data protection:

Information provided in response to this consultation, including personal information, may be subject to publication or disclosure in accordance with the access to information legislation (primarily the Freedom of Information Act 2000, the Data Protection Act 1998 and the Environmental Information Regulations 2004).

If you want information that you provide to be treated as confidential please say so clearly in writing when you send your response to the consultation. It would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded by us as a confidentiality request.

We will summarise all responses and place this summary on our website at www.decc.gov.uk/en/content/cms/consultations/. This summary will include a list of names or organisations that responded but not people's personal names, addresses or other contact details.

Quality assurance:

This consultation has been carried out in accordance with the Government's Code of Practice on consultation, which can be found here:

<http://www.bis.gov.uk/files/file47158.pdf>

If you have any complaints about the consultation process (as opposed to comments about the issues which are the subject of the consultation) please address them to:

DECC Consultation Co-ordinator
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Executive Summary

The EU regulation on wholesale energy market integrity and transparency (REMIT)

- I. The EU regulation on wholesale energy market integrity and transparency (REMIT) prohibits insider dealing and market manipulation in wholesale energy markets and establishes a monitoring regime for wholesale energy trades. The Government created a civil enforcement regime for breaches of REMIT through regulations in June 2013 in Great Britain (it was created in Northern Ireland by regulations that came into force on 31 August 2013). Under this regime, the relevant utility regulator in either Great Britain or Northern Ireland has the ability to require information, carry out inspections, and impose unlimited fines for insider dealing and market manipulation. The regime establishes a new framework for the monitoring of wholesale energy markets to detect and deter market manipulation and insider trading, including introducing an obligation on persons professionally arranging transactions to report suspicious transactions.
- II. We announced in the Annual Energy Statement in October 2013¹, that we would consult on strengthening the existing civil enforcement regime by creating new criminal offences in line with the prohibitions relating to market abuse in REMIT.

Financial market regulation

- III. The UK's regime governing market abuse and inside information in the financial sector consists of both civil and criminal sanctions which are set out by the Financial Services and Markets Act 2000 (FSMA), the Financial Services Act 2012 (FSA), and the Criminal Justice Act 1993 (CJA). These enable the regulator to seek criminal sanctions of up to seven years' imprisonment for market manipulation and insider dealing.
- IV. In EU law, the Market Abuse Directive 2003 (MAD), which was implemented in 2005, required the creation of an EU market abuse regime and a framework for establishing a proper flow of information in the financial markets. It was designed to improve confidence in the integrity of the integrated European market and greater cross border co-operation.
- V. REMIT definitions of inside information (article 3) and market manipulation (article 5) are very similar to those in MAD and existing UK law.
- VI. From 2016, the Market Abuse Regulation (MAR) will replace the MAD. Political agreement was reached on MAR in June 2013 but could not be adopted until certain definitions were agreed through the negotiation of the review of the Markets in Financial Instruments Directive Review (MiFID2).
- VII. The scope of REMIT is partly determined by that definition of financial instruments; contained within MiFID2; therefore REMIT's scope will change when MAR replaces

¹ <https://www.gov.uk/government/publications/annual-energy-statement-2013>

MAD. MAR was published in the EU Official Journal and the majority its provisions will apply from 3 July 2016.

The case for criminal sanctions

- VIII. Articles 3 and 5 of REMIT create prohibitions around insider dealing and market manipulation in wholesale energy markets. These prohibitions equate closely to the criminal offences that already exist in financial markets around market manipulation and insider dealing. Similar behaviour in energy markets can cause similar concerns for consumers and the economy so should be subject to similar sanctions.
- IX. There is a strong case for considering criminal sanctions to support the enforcement of REMIT. Manipulation of energy markets and the misuse of inside information in dealing are significant deviations from normal energy market practices. The wholesale energy markets are opaque at times, as they involve small numbers of highly skilled organisations and individuals using sometimes very technical financial instruments and agreements. This, coupled with the energy market's huge significance for consumers and the economy and the very significant sums of money involved, means that, though the risk of wrong-doing is small, its impact would be significant and would extend beyond the immediate parties to the trade.
- X. The approach we are proposing would give consumers and market participants assurance that the regulator is able to fully address any issues as they arise, and ensure that a more effective deterrent is in place.

We are therefore minded to legislate to create new criminal sanctions around insider dealing and market manipulation as set out in chapters 3 and 4 of this consultation.

Out of scope of proposed criminal offences

- XI. REMIT regulations also place requirements on market participants in articles 4, 8, 9 and 15. For example, articles 8 and 9 deal with registration with the regulator and the provision of information. We are still developing the civil enforcement regime for articles 8 and 9, which is not yet in force. Articles 4, 8, 9 and 15 are about administrative compliance rather than prohibiting activity that directly undermines the efficient and equitable functioning of the regulated market. The civil sanctions, including unlimited fines, are sufficiently severe to have the required deterrent effect on non-compliance with these administrative requirements. On balance, we therefore do not believe that there is a compelling case at present for creating criminal sanctions around these requirements but will keep the effectiveness of the civil sanctions regime for these matters under review.

Approach to Regulation

- XII. In order to ensure that criminal sanctions are in place as soon as possible we are minded to make regulations using the power in section 2(2) of the European

Communities Act 1972 (ECA) to address the clear gap between the financial and energy markets regulatory regimes around insider dealing and market manipulation. Such regulations will only create criminal sanctions with a penalty of up to 2 years imprisonment. The detail of the new criminal offences we are proposing to create around insider dealing and market manipulation is set out in chapters 3 and 4 of this document.

- XIII. We are mindful of the continuing market risks that would be created by the lower maximum prison sentence available to the courts as the sanction that we are proposing for energy market insider dealing and market manipulation compared to the same offences in financial markets (where there is a maximum penalty of 7 years). We are therefore proposing to keep the relationship between the markets under review as the regulatory regime around financial markets develops.
- XIV. We are also proposing to follow the scope of REMIT in terms of the persons captured and extend the offences to include legal persons (companies) and the decision-makers within them.

Civil enforcement

- XV. Enforcement of the proposed new criminal offences will draw on the monitoring and investigatory powers that have been put in place for REMIT civil sanctions. Chapter 5 sets out that existing enforcement regime for REMIT

Responses

- XVI. Responses are invited from all interested parties by 30th September 2014.

Chapter 1: Introduction

- 1.1. We announced in the Annual Energy Statement 2013 that we would consult on the introduction of criminal sanctions for anyone found manipulating energy markets and harming the consumer interest. Competition, transparency and market integrity need to be at the heart of everything we do – this is how we can ensure the best outcomes for consumers.
- 1.2. There need to be tough sanctions for those who break the rules – that is why the UK was amongst the first to implement civil sanctions under new EU REMIT legislation and the Government is now consulting on criminal sanctions for market abuses such as insider dealing.

Wholesale energy markets

- 1.3. The UK wholesale energy markets are of great significance to the UK economy and to Europe as a whole. For example, trading on the GB wholesale energy markets has been estimated to be worth between £297bn – £333.5bn/year. In addition to this figure a significant volume of trading of European energy products is done through London-based brokers. The value of the European gas market being traded through the UK is an estimated £282 billion² in 2013. The UK acts as a hub for gas; the GB liquid gas market is used as a reference price for gas delivered elsewhere in Europe and into the electricity market where gas is a significant and sometimes marginal (price setting) fuel.
- 1.4. The large figures involved and the importance of the wholesale energy market for financial services, industry and UK and European consumers make the integrity of the market a matter of national and international importance.

REMIT

- 1.5. REMIT has been in force since 28 December 2011. REMIT prohibits insider trading and market manipulation in wholesale energy markets across the EU and establishes a monitoring regime for wholesale energy trades by:
 - introducing explicit prohibitions of market manipulation, attempted market manipulation and insider trading in wholesale energy markets;
 - requiring the effective and timely public disclosure of inside information by market participants;
 - introducing an obligation to report suspicious transactions;

- ²Actual brokered over the counter energy data was used (Source: London Energy Brokers Association), plus the additional estimated proportion of that market that is not OTC. This market estimate is for the market from February 2013 until January 2014. Estimates calculated based on the data published by LEBA with the average of the month ahead ICE NBP price.
http://www.leba.org.uk/pages/index.cfm?page_id=4

- establishing a new framework for the monitoring of wholesale energy markets to detect and deter market manipulation and insider trading; and
 - requiring national regulatory authorities (NRAs) to be given enforcement and investigatory powers and requiring member states to establish a penalty regime for sanctioning of breaches at a national level.
- 1.6. The Government’s REMIT enforcement regulations³ entered into force on 29 June 2013. The Northern Ireland REMIT Regulations came into force on 31 August 2013. These regulations together created a civil enforcement regime for market abuse in wholesale energy markets in the UK (hereafter “the 2013 Regulations” or “the civil enforcement regime”). In Great Britain, the regulatory authority responsible for the civil regime is Ofgem; in Northern Ireland, it is the Northern Ireland Authority for Utility Regulation. We use the terms the regulators or regulator to refer to both.
- 1.7. The 2013 Regulations gave the regulators the power to request any relevant information; carry out onsite inspections; and impose unlimited fines for breaches of a REMIT requirement.
- 1.8. Creating the proposed criminal sanctions for energy market abuse and insider trading would be consistent with the implementation that is required by REMIT. REMIT creates requirements and prohibitions mainly on market participants trading wholesale energy and requires Member States to create penalties for breach of the regulation that *are proportionate, effective and dissuasive*. Criminal sanctions are more dissuasive than civil sanctions alone for people who have little to lose from financial penalties or little expectation of on-going engagement in energy markets.
- 1.9. REMIT does not set out how Member States should create penalties for breaches of the regulations. The 2013 regime was put in place to protect consumers from the earliest possible date. At that point it was not practically possible to put in place a criminal regime and so to align more closely with the UK financial services regime.

The scope of REMIT

- 1.10. The scope of REMIT is determined in part by the EU financial regulations. In general terms REMIT covers energy supply and transmission contracts and related derivative contracts. But similar derivative contracts are also covered by energy or financial legislation depending on the platform on which they are traded. As the EU financial regulations are implemented the scope of REMIT will be affected and enforcement for some products may move from Ofgem and the Northern Ireland Authority for Utility Regulation, to the Financial Conduct Authority (FCA). Wholesale energy products are contracts or derivatives, irrespective of where and how they are traded, that are:
- contracts for the supply of electricity or natural gas where delivery is in the EU;

³SI 2013 No 1389 <http://www.legislation.gov.uk/ukxi/2013/1389/made>

- derivatives relating to electricity or natural gas produced, traded or delivered in the EU;
- contracts relating to the transportation of electricity or natural gas in the EU;
- derivatives relating to the transportation of electricity or natural gas in the EU;

except:

- contracts for the supply and distribution of electricity or natural gas to final customers who are a single economic entity where the consumption capacity at any given plant under the control of that single economic entity is less than 600 GWh per year, so far as those plants do not exert a joint influence on wholesale energy prices due to their being located in different relevant geographical markets.

1.11. In addition, Articles 3 and 5 of REMIT do not apply to wholesale energy products which are also financial instruments, to which MAD applies.

Current enforcement arrangements and jurisdiction

1.12. The 2013 regulations create an enforcement regime for listed “REMIT requirements”. The regulations also provide powers and sanctions for the regulator, in order for it to enforce REMIT requirements.

1.13. The 2013 regulations, which draw directly on the underlying provisions of REMIT, should be seen as having the same territorial extent and application as required by REMIT in order to give full effect to REMIT. The regulations could, therefore, extend to offshore activity covered by REMIT, activity where individuals involved in the prohibited activity are present in the UK, or where any relevant wholesale energy product concerns gas or electricity produced in, traded in or delivered to the UK.

1.14. The 2013 regulations give the regulator powers to investigate and monitor energy markets including powers to:

- require regulated persons and others to provide the regulator with information to enable it monitor compliance within REMIT and investigate suspected breaches;
- levy unlimited financial penalties against those in breach of REMIT;
- apply for restitutionary damages to be paid in respect of profits accrued from or losses suffered as a result of failure to comply with REMIT requirement;
- apply for dedicated injunctions to enforce REMIT; and
- enter premises.

Financial regulation

1.15. The UK’s regime governing market abuse and inside information in the financial sector consists of both civil and criminal sanctions which are set out by the FSMA, the FSA and the CJA93 which enable the regulator, amongst other things, to seek

criminal sanctions of up to seven years' imprisonment for market manipulation and insider dealing.

- 1.16. In EU law, the implementation of the MAD in 2005 created an EU-wide market abuse regime and a framework for establishing a proper flow of information to the financial markets. It was designed to improve confidence in the integrity of the integrated European market and greater cross border co-operation.
- 1.17. REMIT definitions of inside information (article 3) and market manipulation (article 5) are very similar to those in MAD and existing domestic legislation.
- 1.18. MAR will now replace the MAD. The draft text of MAR was agreed by the European Commission in June 2013 but could not be adopted until certain definitions were agreed through the negotiation of MiFID2. It is anticipated that MAR will come into force in 2016. MAD (and, in the future, MAR) covers the trading of certain financial instruments. The scope of REMIT is partly determined by that definition of financial instruments contained within MiFID2; REMIT's scope will change when MAR replaces MAD. MAR was published in the EU Official Journal and the majority its provisions will apply from 3 July 2016.

Q1: Consultation Question

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?

Q2: Consultation Question

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

Chapter 2: The Case for Criminal Sanctions

The rationale for creating a criminal penalties regime

- 2.1. There is a strong case for considering criminal sanctions to support the enforcement of REMIT. The wholesale energy markets are opaque at times as they are operated by small numbers of highly skilled organisations and individuals using sometimes very technical financial instruments and agreements. This coupled with the huge significance of energy for consumers and the economy, and the very significant sums of money involved means that, though the risk of wrong-doing is small, its impact would be significant.
- 2.2. We need the highest standard of protection for consumers. Healthy competition in the wholesale energy markets is important. That is why we have put in place a civil sanctions regime with strong incentives not to break the rules.
- 2.3. REMIT creates other requirements for wholesale energy market participants, such as providing information to and registering with the regulator. These are reinforced by the civil enforcement regime that we have put in place.
- 2.4. The prohibited behaviour in relation to market manipulation and insider trading is fundamentally different to a breach of other REMIT requirements because of the potential effect of even a small number of instances of such prohibited behaviour on the functionality and security of the wholesale energy market. We believe that this justifies the labelling of such activity as criminal.
- 2.5. The creation of criminal offences in these circumstances would be proportionate because of the significant harm potentially caused. These prohibited behaviours may have serious financial impact on market participants and on the wider confidence in the operation of gas and power markets, distorting competition and deterring market entry. In addition, there is a real risk that for a small number of organisations or individuals civil sanctions alone may not have a sufficiently strong deterrent effect because there can be very strong incentives to break the rules and it may be possible for those guilty of offences to absorb the civil sanction costs.
- 2.6. Criminal sanctions are more dissuasive where:
 - the market participant is not likely to be a repeat player, for example someone with one-off information about an energy infrastructure problem;
 - a criminal conviction has a particular additional impact on the ability of a person or organisation to conduct business, for example in terms of participation in certain markets or reputational damage from a criminal record; or where
 - financial incentives are not sufficient (for example a person who is already in financial difficulties and feels that they have little to lose). Some individuals and businesses may not be deterred by even unlimited fines. They may have limited funds that could be targeted or may assess that the potential exposure is worth the potential gain. This is likely to be particularly true where

individuals are committing offences such as insider dealing, perhaps in collusion with others, and where their employer is not complicit.

- 2.7. For these reasons, we believe that there is a strong case for putting in place additional criminal sanctions around articles 3 and 5 of REMIT to deal with possible insider dealing and market manipulation. We are therefore minded to use regulations to make sure that the regulator can seek a prison sentence for the worst instances of wholesale energy market abuse.

Q3: Consultation Question

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

Other REMIT requirements and prohibitions

- 2.8. Articles 4, 8, 9 and 15 of the REMIT regulations also place requirements on market participants around market behaviours such as registration with the regulator and the provision of information. We have considered the case for creating criminal sanctions around these requirements, particularly around articles 8 and 9 (registration and the provision of transaction data).
- 2.9. On balance, we do not believe that there is a strong case for putting in place criminal sanctions for these other REMIT requirements at this point. We are still developing the civil enforcement regime for articles 8 and 9, which are not yet in force. But we believe unlimited fines are sufficiently severe to have the required deterrent effect on non-compliance with these administrative requirements. We therefore do not believe that there is a compelling case at present for creating criminal sanctions around these requirements but will keep the effectiveness of the civil sanctions regime for these matters under review.

Q4: Consultation Question

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?

Approach to regulation

- 2.10. The criminal sanctions regime we are proposing could be put in place by March 2015 using section 2(2) of the European Communities Act 1972 (ECA). Using the

ECA would however mean a maximum of 2 years imprisonment could be imposed by courts.

- 2.11. This is less than the maximum penalty of 7 years imprisonment available for the most serious instances of insider dealing and market manipulation in financial services.
- 2.12. Putting in place criminal offences with longer maximum sentences would require primary legislation, and that would take considerably longer to implement. Given the risks to market participants and consumers attached to the absence of any criminal sanctions for energy market manipulation and insider dealing, we are minded to make regulations under the ECA by early 2015.
- 2.13. We are however mindful of the arguments that there is a continuing market risk created by the lower maximum sanction we are proposing for energy market insider dealing and market manipulation compared to financial markets. We therefore propose keeping the relationship between the wholesale energy and financial market regulatory frameworks under review as the regulatory regime around financial markets develops. If a compelling case for equalisation of the sanctions available for similar criminal behaviours emerges then we would bring forward further proposals.

Alignment with financial services legislation

- 2.14. A coherent relationship between the regulatory regimes for energy markets and financial markets is important to ensure consistency of treatment and effective deterrence. Without a common approach there is a risk that people will apply lower standards of market conduct in the energy market because it does not have criminal sanctions.
- 2.15. Currently, the UK's regime governing market abuse and inside information in the financial sector consists of both civil and criminal sanctions and is set out by the FSMA, the FSA and the CJA, together with the Financial Conduct Authority Handbook⁴.
- 2.16. The implementation of REMIT should be seen against the backdrop of the development of EU financial legislation which is tightening the regulation of financial markets. The proposed EU financial legislative instruments closely linked to REMIT are contained within MIFID2 and MAR. The Commission also adopted a proposal for a regulation on indices used as benchmarks in financial instruments and financial contracts on 18 September 2013⁵.
- 2.17. We therefore intend to keep the relationship between energy market and financial market regulation under review with the aim of increasing their alignment over time.

⁴ <http://fshandbook.info/FS/html/FCA/>

⁵ http://ec.europa.eu/internal_market/securities/benchmarks/index_en.htm#maincontentSec1

Chapter 3: Insider trading

The REMIT prohibition

- 3.1. Insider trading focuses on the misuse of non-public information that may affect the trade in a wholesale energy product. In financial services trading based on inside information is illegal because it is seen as being unfair to other investors who do not have access to the same information. The principal domestic criminal offence for the insider trading of financial products is in Part 7 of the CJA which applies to natural persons (individuals) only.
- 3.2. Persons who possess inside information in relation to a wholesale energy product are prohibited by Article 3 of REMIT from buying or selling relevant energy products, disclosing the information or influencing someone else to buy or sell the products.

The proposed criminal offence

- 3.3. The current civil enforcement regime relies on breaches of prohibitions set out in REMIT. In order to create a clear and proportionate criminal offence, it is necessary to define the elements of any offence within UK law. This and the following sections therefore make a set of detailed proposals and raise issues that would need to be addressed in creating a criminal offence framework.
- 3.4. We are minded to make regulations such that a person commits the offence of insider dealing if they:
 - use inside information to acquire or dispose of wholesale energy products to which that information relates, either on their own account or on behalf of others;
 - disclose inside information except in the normal course of his duties; or
 - use inside information when recommending that another person acquire or dispose of wholesale energy products, or when inducing them to deal in wholesale energy products.

Inside information

- 3.5. We propose that “inside information” should be defined in accordance with REMIT so as to cover information which:
 - relates, directly or indirectly, to one or more wholesale energy products,
 - is specific or precise – information would be precise if it indicates:
 - a set of circumstances which exists or may reasonably be expected to come into existence, or
 - an event which has occurred or may reasonably be expected to do so, and

if it is specific enough to enable a conclusion to be drawn as to the possible effect of that set of circumstances or event on the prices of wholesale energy products;

- has not been made public; and
- would be likely to significantly affect the prices of those wholesale energy products if it were made public.

3.6. For the purposes of the proposed offence “information” would mean:

- information which is required to be made public in accordance with Regulations (EC) No 714/2009 and (EC) No 715/2009, including guidelines and network codes adopted pursuant to those regulations;
- information relating to the capacity and use of facilities for production, storage, consumption or transmission of electricity or natural gas or related to the capacity and use of Liquefied Natural Gas (LNG) facilities, including planned or unplanned unavailability of these facilities;
- information which is required to be disclosed in accordance with legal or regulatory provisions at EU or national level, market rules, and contracts or customs on the relevant wholesale energy market, in so far as this information is likely to have a significant effect on the prices of wholesale energy products; and
- other information that a reasonable market participant would be likely to use as part of the basis of its decision to enter into a transaction relating to, or to issue an order to trade in, a wholesale energy product.

Who could it capture?

3.7. One aspect of creating a criminal offence on which it is necessary to be clear is those persons who might commit the offence. While it is probable that a person committing insider trading or manipulating energy markets would have some professional role in or link to those markets, it is not a certainty and REMIT consequently prohibits insider trading by a wider range of persons. We are therefore proposing that a person committing the new offence of inside dealing could be any natural or legal person (e.g. a company) and, where it is a legal person, the natural persons deemed party to the decision (see the discussion of our proposal on legal persons below).

3.8. Where they are a natural person, they could be:

- a director or employee of an organisation;
- a shareholder of an organisation;
- a person with access to the information by virtue of their employment, office or profession;
- a person who has acquired such information through criminal activity; or
- a person who knows, or should reasonably know, that it is inside information.

What behaviours would be captured?

3.9. In order to create criminal offences under UK law around the REMIT prohibitions we need to set out how the prohibited behaviours would be framed. We are proposing that:

- “Acquire”, in relation to a wholesale energy product, would include
 - agreeing to acquire the wholesale energy product; and
 - entering into a contract which creates the wholesale energy product.
- “Dispose”, in relation to a wholesale energy product, includes:
 - agreeing to dispose of the wholesale energy product; and
 - bringing to an end a contract which created the wholesale energy product.

Territorial link to the UK

3.10. In framing a new criminal offence in the UK we need to be clear about its geographic scope. The scope of REMIT is very broad, as is befitting an EU regulation which seeks to put in place a regime standardizing the regulatory approach to a large and complicated market. Therefore, within the UK, all activity covered by REMIT is prohibited.

3.11. However, making any breach of REMIT a criminal offence in the UK wherever it occurs within the EU would have significant ramifications and would in our view be a disproportionate use of the UK criminal jurisdiction. To limit the subject matter of the trades to only those where the delivery is in the UK would fail to take into account the importance of the UK as a trading centre.

3.12. We consider it justifiable to focus criminalization on activities prohibited by article 3 of REMIT with a clear UK element. Therefore, the prohibited activities of “acquiring”, “disposing”, “disclosing”, “recommending” or “inducing” should take place, or the effect should be, in the UK.

3.13. We therefore propose that any of the following (and more than one may be present in a particular criminal activity) would be sufficient to justify prosecuting an offence in the UK:

- Acquiring or disposing of a REMIT product where:
 - the defendant (which could be any party to the trade) is in the UK or is registered with a UK energy regulator;
 - the gas or electricity being traded originates in, is for delivery in, or transits through the UK; or
 - the transaction takes place in UK (for instance, on a trading platform based in the UK or is subject to a jurisdiction clause in favour of a UK legal jurisdiction).
- Disclosure of price sensitive information about a REMIT product where:
 - the gas or electricity being traded originates in, is for delivery in, or transits through UK;

- the defendant disseminating is in UK, or is registered with a UK energy regulator; or
 - the defendant is outside UK but the alleged recipient of the dissemination is in UK.
- 3.14. Where recommending or inducing another person to acquire or dispose of a REMIT product where:
- the defendant person recommending or inducing is in UK, or is registered with a UK energy regulator;
 - the defendant is outside UK but the alleged recipient of the recommendation or inducement is in UK;
 - the subject matter gas or electricity originates in, is for delivery in or transits through the UK; or
 - 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 legal jurisdiction).
- 3.15. REMIT potentially covers activity that is conducted offshore and outside the normal 12 nautical miles territorial limit. We think that the territorial extent of the activity covered in the criminal offences we are proposing should mirror that of the REMIT obligation on the UK, and therefore activity that occurs offshore but within the UK's jurisdiction would be capable of being within the criminal offence.

Fault element for activity prohibited under article 3 of REMIT

- 3.16. When creating a new criminal offence it is necessary to consider whether a degree of fault, if any, should to be required in relation to the prohibited activity. Criminalisation shows that a particular activity undertaken was of a sufficiently serious nature that the person undertaking that action should be labelled a criminal. We also think that criminal sanctions should focus on serious breaches of the general prohibitions in REMIT – which are also enforceable through civil mechanisms under the 2013 Regulations.
- 3.17. There are two options for creating a fault element:
- a general prohibition with a defence for acceptable (innocent) behaviour; or
 - a restriction on the scope of the required mental element (that is whether the person should intend to or be reckless as to committing a criminal offence).
- We are proposing to adopt the second approach, requiring a mental element.***
- 3.18. Under this approach it is clear that a person should have acted in a blameworthy manner. It then expresses the nature of blameworthy action and places the evidential burden with the prosecution. If there is to be a mental element, then there are the following options:
- intentional only;
 - intentional and/or reckless activity.

- 3.19. In these circumstances, intentional means taking action knowing that it is prohibited (for example, knowingly engaging in the disclosure of inside information). Reckless, for these purposes, means undertaking a particular course of action aware that it could amount to the prohibited activity (a prohibited disclosure), even if this is not the desired outcome, but knowing that such might occur. If only intentional activity was criminalised, this would be different to other areas of financial services where reckless behaviour is also criminalised.
- 3.20. Moreover, restricting offences only to intentional behaviour would not encapsulate some of the activity that we wish to protect against. For instance, it would be necessary to include recklessness in order to criminalise instances of insider dealing which, while not obviously intentional, ought to have been expected. This would include instances where a “blind eye”, whether wilful or not, has been turned to insider dealing. We are therefore proposing that the insider dealing offence should only apply where the insider dealing is conducted either intentionally or recklessly.

Exemptions

- 3.21. If a criminal offence is drawn too broadly it risks capturing some activities that we would not want to criminalise because they are vital for the effective functioning of the wholesale energy market or the security of wholesale energy supplies. This section sets out our proposals for exemptions that should apply and defences that may be invoked so that necessary or permissible activities do not incur a criminal sanction.
- 3.22. The exemptions we are proposing are where a person:
- (for offences other than disclosure) is a transmission system operator purchasing electricity or natural gas in order to ensure the safe and secure operation of the system in accordance with his obligations under points (d) and (e) of Article 12 of Directive 2009/72/EC or points (a) and (c) of Article 13(1) of Directive 2009/73/EC;
 - is acting under national emergency rules;
 - disseminated the information for the purposes of journalism or artistic expression unless:
 - he derived or might reasonably have expected to derive, directly or indirectly, an advantage or profits from any impact on the price of a relevant product from the dissemination of the information in question; or
 - the disclosure or dissemination is made with the intention of misleading the market as to the supply of, demand for, or price of wholesale energy products;
 - conducted a transaction in the discharge of an obligation that has become due to acquire or dispose of a wholesale energy product where that obligation results from an agreement concluded, or an order to trade placed, before he came into possession of inside information; or
 - is an electricity or natural gas producer, an operator of a natural gas storage facility, or an operator of a LNG import facility who

- entered into the transaction solely to cover the immediate physical loss resulting from unplanned outages, where not to do so would result in a market participant not being able to meet existing contractual obligations or where such action is undertaken in agreement with the transmission system operator in order to ensure safe and secure operation of the system, and
- has reported the transaction to the appropriate regulatory body.

Q5: Consultation Question

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

Q6: Consultation Question

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

Legal persons and the officers of legal persons

- 3.23. We are proposing that the offence of insider dealing in wholesale energy market products includes companies, and the individuals who participate in decision-making within them. Though this is not the approach taken in the existing insider dealing offence for financial services, it is consistent with the requirements of REMIT – where the prohibition on insider dealing extends to companies (legal persons) and individuals (natural persons).
- 3.24. We believe that the offences described above, if applied to legal persons and natural persons, will create a significant deterrent to insider dealing over that provided by the civil enforcement regime. In addition to the significant impact of a conviction under the civil regime for REMIT, a criminal conviction for a corporate person would have an impact on its ability to pursue its business in some countries.
- 3.25. In particular, we believe that the possibility of criminal prosecution for recklessly insider dealing will act as a clear and powerful incentive to those organisations that could potentially profit from such activity to create strong processes to deter and detect any breaches.

Q7: Consultation Question

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

Chapter 4: Market Manipulation

- 4.1. Market manipulation is the interference or the attempt to interfere with the free and fair operation of the market and create artificial, false or misleading appearances with respect to the price of, or market for, a security, commodity. Article 5 of REMIT prohibits market manipulation. We are minded to strengthen the regime of civil sanctions with a new criminal sanction that the regulator can seek for the most serious offences.

The proposed offence

- 4.2. We are proposing that an offence of energy market manipulation will have been committed if a person:

- makes a false or misleading statement,
- conceals a fact, or
- creates a misleading impression

which is liable to induce another person to take certain actions relating to a wholesale energy product or the rights it confers.

- 4.3. We propose that a person would also be liable for attempting to manipulate the wholesale energy market.

- 4.4. A person would have committed the offence if they:

- enter into or refrains from entering into any transaction or issues or refrain from issuing any order to trade in wholesale energy products which —
 - give, or are likely to give, false or misleading signals as to the supply of, demand for, or price of wholesale energy products;
 - secure or attempt to secure, by a person, or persons acting in collaboration, the price of one or several wholesale energy products at an artificial level; or
- employ or attempt to employ a fictitious device or any other form of deception or contrivance which gives, or is likely to give, false or misleading signals regarding the supply of, demand for, or price of wholesale energy products; or
- disseminate information which gives, or is likely to give, false or misleading signals as to the supply of, demand for, or price of a wholesale energy product, where they knew, or should reasonably have known, that the information was false or misleading.

Territorial link to the UK for market manipulation

- 4.5. As with the discussion set out in the preceding chapter on insider trading, it is necessary to set out the territorial scope of the new offence and we suggest that there needs to be a clear link to the UK jurisdiction in order to put in place a clear and proportionate criminal offence of market manipulation.

- 4.6. We, therefore, propose that the presence of one of the following would be sufficient to provide such a link:
- Entering into transaction to give false or misleading impression where:
 - the defendant (which could be any party to the trade) is in the UK or is registered with a UK energy regulator;
 - the gas or electricity being traded originates in, is for delivery in, or transits through the UK; or
 - the transaction takes place in UK (for instance, on a trading platform based in the UK or is subject to a jurisdiction clause in favour of a UK legal jurisdiction).
 - Disseminating information which gives or is likely to give a misleading impression where:
 - the subject matter gas or electricity originates in, is for delivery in, or transits through UK;
 - the defendant person disseminating is in UK, or is registered with a UK energy regulator; or
 - the defendant is outside UK but the alleged recipient of the dissemination is in UK.

Fault element for energy market manipulation

- 4.7. As with the criminal offences relating to insider dealing, we consider that there should be a fault element for criminal market manipulation. This, in the same manner as described above, is necessary to ensure proportionality in applying a criminal sanction and as a marker that the behaviour is truly blameworthy
- 4.8. The prohibited activities for market manipulation outlined above would have to have been conducted either intentionally or recklessly.
- 4.9. We do not believe that only criminalising intentional behaviour is sufficient, as it fails to adequately capture some of the damaging behaviours that could distort a market undertaken by those who know that their activity may have such an effect.

Exemptions

- 4.10. As with the exemptions and defences set out in Chapter 3, we need to state clearly any behaviour which would not incur criminal sanctions because they are necessary for the functioning of the energy system including its markets or are otherwise permissible. We are minded to create exemptions to the offence of energy market manipulation such that a person is not committing the offence of energy market manipulation if he:
- establishes that his reasons for entering into the transaction or issuing the order to trade are legitimate and that that transaction or order to trade conforms to accepted market practices on the wholesale energy market concerned

- is acting under national emergency rules;
- disseminated the information for the purposes of journalism or artistic expression unless:
 - he derived or might reasonably have expected to derive, directly or indirectly, an advantage or profits from any impact on the price of a relevant product from the dissemination of the information in question; or
 - the disclosure or dissemination is made with the intention of misleading the market as to the supply of, demand for, or price of wholesale energy products.

Benchmark manipulation

- 4.11. Benchmarking is an aspect of markets that could be particularly sensitive to manipulation. The benchmarking process can draw on a comparatively small number of trades to establish reference prices that are made use of by a much larger number of market participants and products. This amplifying effect naturally makes the fair operation of benchmarks a matter of significant public concern. The REMIT prohibition on market manipulation covers the manipulation of markets through the manipulation of benchmarks. Such manipulation could be:
- providing false information to undertakings which provide price assessments or market reports with the effect of misleading market participants acting on the basis of those price assessments or market reports; or
 - offering, buying or selling wholesale energy products with the purpose, intention or effect of misleading market participants acting on the basis of reference prices
- 4.12. There is a high level of risk and therefore a high degree of public concern around the manipulation of benchmarks. Subject to the responses received to this consultation, and to Ofgem and the Northern Ireland Authority for Utility Regulation's views in response to its call for evidence on benchmarks, ***we are proposing that the offences of energy market manipulation include the manipulation of benchmarks.***

Q8: Consultation Question

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

Chapter 5: Enforcement

- 5.1. UK regulations for the civil enforcement regime for REMIT came into effect in June 2013 and August 2013. The new criminal offences we are proposing here would draw on powers of monitoring and investigation contained in those regulations.
- 5.2. We set out below for information only those powers that enable the regulator to monitor transactions and investigate potential breaches of REMIT as they underpin the regulator's investigations, and may result in a prosecution for the criminal offences proposed above. We are not consulting here on giving the regulator any further powers or placing any further requirements on market participants as part of this consultation on REMIT criminal offences.

Monitoring and investigatory powers

- 5.3. The regime requires regulated persons to retain and record documents and information. The regime also allows the regulator to commence an investigation if there are circumstances suggesting that there has been a breach of a REMIT requirement. This includes the prohibition on insider trading, obligation to publish inside information, prohibition of market manipulation and obligations of persons professionally arranging transactions, as set out in articles 3, 4, 5 and 15 of REMIT. To facilitate an investigation, the regulator is able to request any relevant information or documents from any relevant person.
- 5.4. The regulations give the regulator a limited power of entry under a warrant issued by a court. The regulator is only able to apply for a warrant where it has not been possible to obtain information using its existing information gathering powers or, for example, where it is likely that information relevant to an investigation would be destroyed.
- 5.5. To ensure that market participants comply with an information request by the regulator the enforcement regulations include criminal offences relating to the enforcement provisions. These provisions deal with failures to comply with a requirement to provide information or documents (without reasonable excuse), falsifying, concealing, destroying or otherwise disposing of a document and knowingly or recklessly providing false or misleading information.

Sanctions and injunctions

- 5.6. The civil enforcement regulations allow the regulator to impose, and determine the amount of, a financial penalty, if it finds a breach of the REMIT prohibitions. Furthermore, the regulator may publish a statement to the effect that a person has failed to comply with a REMIT requirement. In order to provide clarity on the penalties that will apply to breaches of REMIT, the regulations require the regulator to consult on and issue a statement of its policy. Ofgem published its

penalties statement⁶ and procedural guidelines⁷ for REMIT on 8 November 2013. Alternatively, the regulator may apply to the High Court (or, in Scotland, the Court of Session) to impose a penalty. The regulator may only do this if also applying for an injunction or restitution order.

- 5.7. There are also provisions allowing for the regulator to seek injunctions and restitution orders.
- 5.8. The provisions give the regulator the power to apply for a court order requiring the cessation of any practice that is contrary to REMIT, preventing a person from disposing of assets, or temporarily suspending professional activity. The court may also be asked to require a person in breach of a REMIT requirement to take remedial steps. This aligns with the financial markets regulatory regime.
- 5.9. The UK REMIT civil enforcement regime sets out that, if there has been a breach of a REMIT requirement and the person found in breach has accrued profits, or one or more persons have suffered loss, then the person in breach may be required to make restitution. This power is exercisable either by the court or by the regulator.

Q9: Consultation Question

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?

Q10: Consultation Question

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

⁶ <https://www.ofgem.gov.uk/ofgem-publications/84346/remitpenaltiesstatement8november2013.pdf>

⁷ <https://www.ofgem.gov.uk/ofgem-publications/84347/remitproceduralguidelines8november.pdf>

Glossary

REMIT	EU Regulation on Wholesale Market Integrity and Transparency
MiFID	Markets in Financial Instruments Directive
EMIR	European Markets Infrastructure Regulation
MAD	Market Abuse Directive
CSMAD	Criminal Sanctions Market Abuse Directive
CJA	Criminal Justice Act 1993
FSA	Financial Services Act 2012
FCA	Financial Conduct Authority
FSMA	Financial Services Markets Act 2000
Ofgem	Office of Gas and Electricity Markets

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