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20 November 2012

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Submission on Initial Margin Methodology Review

Genesis Power Limited, trading as Genesis Energy, welcomes the opportunity to provide a submission to the Clearing Manager on the consultation paper "Clearing Manager Financial Transmission Rights Prudential Security Initial Margin Methodology Review" dated 23 October 2012.

Genesis Energy's responses to the consultation questions are in Appendix A.

If you would like to discuss any of these matters further, please contact me on 04 495 3340.

Yours sincerely

Jeremy Stevenson-Wright
Regulatory Affairs Manager

Appendix A: Responses to Consultation Questions

QUESTION	COMMENT
A. What, if any, role is appropriate for ASX prices in considering initial margin requirements?	ASX prices appear to have a supplementary role in providing some guidance around expected conditions given specific hydrology and other market factors. We recommend that ASX prices are used in combination with, or as an input to, the other modelling approaches discussed in the consultation paper.
B. Do you support a fixed initial margin based upon an analysis of PLGD for each FTR product and season or do you support an alternate aggregation?	The paper does not describe well how the observed ASX volatility aligns with historic price based implied FTR settlements. Therefore, it is not clear that the particular approach to seasons is the most efficient. However some form of sculpting appears to be generally representative of market risk and volatility.
C. In calculating PLGD what time frame should be considered? (10 or 21 days, or other)	We consider the PLGD period for a period of at least 21 days is the most appropriate. Any prudential time frame must be consistent with NZEM prudential arrangements so as to not compromise any relative efficiency. We consider it is important that the timeframes align, in as much as possible, with those under consideration by the Electricity Authority as part of the settlement and prudential review. The Authority has yet to make a decision on implementing recommendations from the Wholesale Advisory Group.

QUESTION	COMMENT
D. What is an appropriate PLGD confidence interval to apply in order to determine the FTR initial margin requirement (95%, 85%, 75% other)?	We consider that 75% seems like a reasonable number given the history of the market, the overall desire to grow participation in the FTR market, and the presence of other prudential arrangements (such as variation margins).
E. Should the initial margin requirements be based upon changes in the expected value of FTR instruments as forecast by the predictive price model?	Yes. However, we note that without data from the predictive price model it is difficult to assess the efficiency of this proposal. In particular, care needs to be taken to ensure that market bidding behaviour does not become model driven as a result of this approach. We suggest that the Clearing Manager must be aware of this potential risk, and should take steps to monitor it.
F. Should the initial margin requirements be recalculated six monthly starting from the date of the first auction using the described methodology?	It is difficult to comment on the appropriate recalculation timeframe without further information on the underlying drivers . However, in the absence of this information, six months seems a relatively sensible place to start.
G. Should the initial margin requirement be recalculated one week prior to the first auction, and the lesser of the recalculated requirement or the requirement published in this paper used?	We agree that this proposal has the potential to increase participation in the FTR market and improve efficiency of the prudential system. However, a consequence of this proposal is that prudential requirements may lower prudential requirements are applied to participants who subsequently default.

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