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Ian Dempster
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Dear Ian

Wholesale Market Design – Follow-up Paper

Genesis Power Limited, trading as Genesis Energy, welcomes the opportunity to provide comments to the Gas Industry Company on Part Two of its discussion paper on Wholesale Market Design dated December 2006. Genesis Energy has reviewed the discussion paper and is pleased to have the opportunity to respond to the issues raised in it.

In general, Genesis Energy welcomes the Gas Industry Company's approach to the continued development of the wholesale gas market and fully supports the principles against which the Gas Industry Company will analyse the options for developing a voluntary matching platform to facilitate short term gas trading. As the platform will support a small and developing market which will involve physical delivery, it will be crucial that delivery is made as simple as possible otherwise it will be difficult for the platform to develop.

If you would like to discuss any of these matters further please contact either myself on 021 375 061, or Roger Johnston on 09 580 4917.

Yours sincerely

John A Carnegie
Regulatory Affairs Manager
Genesis Energy

Appendix One: Responses to Specific Consultation Questions

QUESTION	COMMENT
Q1: Do you agree that user pays is the preferred option for funding the establishment and ongoing operation of a wholesale market for gas? If not, what funding mechanism do you consider most appropriate and why?	As the Gas Industry Company itself recognises there are a number of mechanisms via which the costs (both initial set up and on-going) can be recovered. In general, Genesis Energy supports an approach that is more akin to 'beneficiary pays' rather than user pays. The underlying principle in this regard is that those who benefit from the development of the trading platform should incur the cost of it in proportion to their use. Ultimately, the beneficiaries are expected to be end consumers given the expectation that the trading platform will more efficiently allocate gas thereby placing downward pressure on the overall market price of gas – and this benefit clearly accrues to all customers irrespective of whether their specific gas has been traded on via the platform in proportion to their gas use. The key issue, of course, is how best to translate such a principle into a workable and low cost recovery mechanism. In this regard, Genesis Energy has the following suggestions: 1. it is appropriate to differentiate between development costs and on-going operating costs; 2. ultimately, all costs should be recovered in proportion to consumption under the Gas Industry Company's levy via a $/GJ charge that can be passed through to end customers; 3. with respect to development costs, while these should ultimately be recovered via a levy of the nature described in 2. above, they should <u>not</u> be recovered in the first year. This is consistent with the expectation that the platform will be long-lived and its benefits spread over a period of greater than one year. In addition, the beneficiaries in year one may not be the beneficiaries in out-years. These factors suggest that the Gas Industry Company should finance the development costs and recover the financing costs over the life of the loan. This will avoid the prospect of a 4% increase in the levy as suggested could eventuate in paragraph 7.15 of the discussion paper; and

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	4. with respect to the on-going costs, it might be expected that there would be two components to these costs – these being transaction-based charges and the recovery of the annual fixed costs (such as depreciation and maintenance costs). Given the likely web-based nature of the platform, Genesis Energy expects the transactional costs to be extremely small and difficult to individually attribute and so should be aggregated into the annual fixed costs. Consistent with Genesis Energy's view that end customers are the beneficiaries and the position set out in 2. above, these charges too should be recovered under the Gas Industry Company's levy via a $/GJ charge.
Q2: Do you support the proposed approach to admission? If not, what alternative would you want and why?	Genesis Energy agrees that the admission process should be kept as simple as possible so that the platform is available to as wide a group of participants as possible and that development costs are minimised. Genesis Energy agrees that set up costs for an entrant should be recovered by a standard fee.
Q3: Do you support the proposed approach to suspension? If not, what alternative would you want and why?	Genesis Energy also supports the proposed approach to suspension. Parties will be able to manage their exposure to individual market participants through the proposed white list prudential process however where a party defaults on its obligations under the "Deed of Participation" (see Q10 below) then other participants should be protected either by notification of the default or suspension of the offender.
Q4: Do you support the proposed approach to user controls? If not, what alternative would you want and why?	Genesis Energy supports the proposed approach to user controls. The provision of an administrator role, limitations on trading authorities and confirmation of trades to user company back office systems of trades is sufficient to manage risks in this area. Participants should be required to back any transaction undertaken by an individual qualified by that participant.
Q5: Do you support the proposed approach to display of bids/offers? If not, what alternative would you want and why?	Genesis Energy supports a blind market with participants seeing all bids and offers with matching being managed through a white list prudential process. Costs of system development and operational costs will escalate if more complex processes involving margin calls for example are introduced. Genesis Energy would view an "override" as a 'nice-to-have' but only if the cost of providing the option is minimal.

QUESTION		COMMENT
Q6:	Do you support the proposed form of prudential criteria? If not, what alternative would you want and why?	In Genesis Energy's view, parties should manage their trading limits with other market participants through their own internal risk management systems and processes. Accordingly the prudential criteria (including monetary and volume limits) do not need to form part of the platform process. Adding this type of functionality into the platform at this stage is not necessary and is not consistent with a simple matching platform and the separation of processes as set out in section 8.4 of the paper.
Q7:	Do you support the proposed approach to adjusting prudential criteria? If not, what alternative would you want and why?	In line with Genesis Energy's response to Q6 above, this functionality does not need to part of the platform. So long as the platform allows participants to modify their white-list on a timely basis (e.g. at times when the platform is not trading) that does not allow gaming then that should be sufficient.
Q8:	Do you support the proposed provision of an override? If not, what alternative would you want and why?	See response to Q5 above. The platform should operate with the participants having some confidence that the range of possible counterparties is reasonably stable across trading periods.
Q9:	Is your use of a platform likely to be significantly affected by whether the market operated on a blind basis or not? If so, in what way?	A blind market minimises the risks of participants gaming the market and is preferred for increased liquidity. If the market is not blind then it is very likely that it will be bypassed by direct bilateral trading leaving the platform as a notice board only.
Q10:	Do you support the underlying philosophy in relation to the nature of the rights and obligations associated with a trade? If not, what alternative would you want and why?	The trading process as set out on page 29 appears to miss the initial requirement for a "Deed of Participation" that a party would enter into as part of the admission process. This deed would encompass such things as the platform governance process, the standard contract, platform trading hours, time periods that are traded etc with a key item being the obligation on a party to enter into the bilateral agreement (standard contract) if its bid or offer is matched on the platform. Once the standard contract is executed by the two "matched" parties its terms then covers the obligations to deliver and pay etc.
Q11:	Do you support the proposed provision of buy and sell offers? If not, what alternative would you want and why?	Market participants are likely to include gas producers, wholesalers, retailers and end users. Some parties may only be able to be on one side due to the physical delivery requirements of the market and the requirements for transmission arrangements to effect delivery. Therefore, participants should have the flexibility to make either buy or sell offers or both for any period.

QUESTION	COMMENT
Q12: Do you support the proposed use of 0.1 TJ/day as the basic trade unit? If not, what alternative would you want and why?	In Genesis Energy's view, 0.1TJ is too small an amount. Instead, Genesis Energy proposes that a contract is for 1TJ. If a party is able to know their gas position down to the level of 0.1TJ on a day then they are unlikely to require access to a balancing market! Such a small contract volume will also increase the level of back office administration. A contract volume of 1TJ is consistent with tolerances provided under the MPOC which range from 3 – 10TJ.
Q13: Do you support the proposed ability to indicate whether partial acceptances will be permissible? If not, what alternative do you prefer and why?	Partial acceptances should be a standard feature of the platform rather than an option. If for example a seller is offering to sell five contracts it is very unlikely that they would not want to sell 3 if that is all a buyer wanted.
Q14: Do you support the proposal to adopt a virtual trading point? If not, what alternative do you prefer and why?	Delivery has to be made as simple as possible for the matching platform to have any chance of success. Genesis Energy fully supports the development of a dedicated virtual Matching Platform Welded Point ("MPWP") on the Maui pipeline to facilitate delivery. Such a welded point by definition has to be balanced every day and as the volumes are likely to be small relative to total volumes being shipped on a day consideration could also be given to giving nominations to and from the welded point some level of priority in the event of MPOC curtailments etc. This may help promote the development of the market. The location the MPWP could, for example, encompass the receipt points from Frankley Road in the south to Tikorangi in the north. Arrangements would need to be made with MDL so that tariff 2 only applied once- that is, either to gas when nominated to or from the MPWP.
Q15: What sort of information would your organisation want from a platform for trading purposes?	The platform will need to enable a party to easily identify all of its live bids and offers for each of the traded time periods. On the matching of a trade, the matching platform needs to provide a party to a trade with details of buyer and seller, period (day) of the trade, price, and number of contracts. The timing of the provision of such information will depend on when the platform closes off for trades for a day. If, for example, the platform closes off at midday on the day prior to the day of delivery then the platform has to be able to provide the above information within a couple of hours so that nomination processes can be initiated.

QUESTION	COMMENT
Q16: What sort of information would your organisation want from a platform for billing, reporting and governance purposes?	See the response to Q15 above. In addition, the provision of day ahead position reports at the close of trade including volume weighted price, open-high-low-close-volume reports covering each or the periods traded
Q17: What sort of information should a platform provide for general dissemination to stakeholders?	Volume weighted average prices (bid and offer and actual trades (based on a minimum number of trades being done).