

Impacts On Power & Gas Marketing

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IPR-GDF SUEZ Energy Marketing North America, Inc.

“The Impact of Dodd-Frank on Energy Trading”
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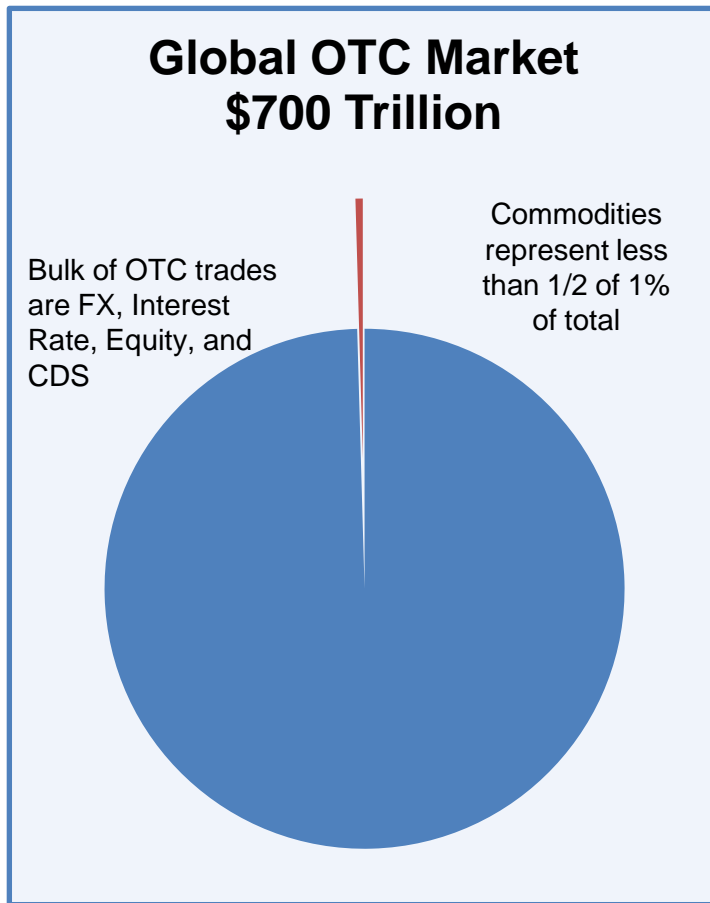


IPR-GDF SUEZ North America Profile

- 14,000 MW of electricity generation; 77 power plants
- Top 5 C&I electricity retailer in 12 states
- No. 1 importer of LNG into the US
- No. 2 gas pipeline company in Mexico
- No. 2 LDC operator in Mexico
- Stock symbol IPR on LSE
- Credit support from GDF Suez, largest independent power producer in the world, rated A by S&P



DFA Profoundly Affects The OTC Energy Market



After 2008 Financial Crisis,
Derivatives = Political Target

DFA creates new wave of
regulations

Principal Industry Concerns

- Short Deadlines/High Ambiguity
- Regulatory Burden
- Compliance Costs
- Unpredictable unintended consequences

Source: *Bank for International Settlements, "OTC derivatives market activity in the first half of 2011" (16 Nov 2011)* available at www.bis.org/statistics/derstats.htm

IPR-GSEMNA Classification Currently An Unknown



Expect Final
CFTC Rules
Mar/Apr 2012

Scenario I: Eligible Contract Participant
(*currently viewed as More Likely*)

ECP below SD threshold as

- *company regularly engages in swaps*
- *aggregate notional values < \$3 Billion excluding hedges [not certain]*

Scenario II: Swap Dealer

- (*possible if definitional threshold is lower than \$3 billion or doesn't exclude hedges*)

Compliance Obligations

- Business conduct rules, centralized clearing/margining, capital requirements and reporting, registration, Chief Compliance Officer

Impacts To The Business Model



- Can we optimize credit by using a central entity to conduct hedging on behalf of affiliates?
- Reassess hedging policy
 - If costs of hedging goes up, should we hedge to same degree /in same way?
- Reassess mix between hedging and trading
- How do we ensure compliance with Position Limits rule with foreign affiliates and minority interest entities?
- Are we adequately staffed?
- How much will it cost?

Impacts To The ETRM Systems

- Significant effort required to design set of new compliance processes and enhance the IT and reporting systems
- New pre-trade processes
- Smart routing of trades to clearinghouses
- New post-trade external data communications and reporting
- Action plan may require up to 1 year for implementation of planned changes, depending on extent of enhancements required



Impacts To Capital And Credit Management



How much capital (if SD) and cash is required?

Daily margining at DCOs
Routine example

- Assume a typical 500 MW CCGT plant to be built in Texas, COD 2015. Plant Cost: \$550 Million; Hedge Plan: hedge spark spread (buying gas/ selling power) for three years; capacity factor 50%, 7200 MMBtu/MWh, \$30/MWh spark spread, \$4.35/MMBTU natural gas; 30% volatility; assume no netting

Notional Value of Hedges: \$640 M
*Range of Cash Collateral
Required* \$96 - \$430 M

Credit and cash optimization will be increasingly important

Likely Impacts To Power & Gas Markets



Increased cash intensity from central clearing will cause some participants to exit

Less market depth and breadth means wider bid/ask spreads and more volatility

Volcker rule may cause Banks to withdraw from less liquid markets (e.g. ERCOT)

Cash intensity will cause some participants to shorten their hedging tenors

Impacts to Power & Gas Transactions



Definition of swaps not yet issued

- Potential issues -- physical power and gas transactions with imbedded options

Know your counterparty, and what his/her intent is – hedging or trading

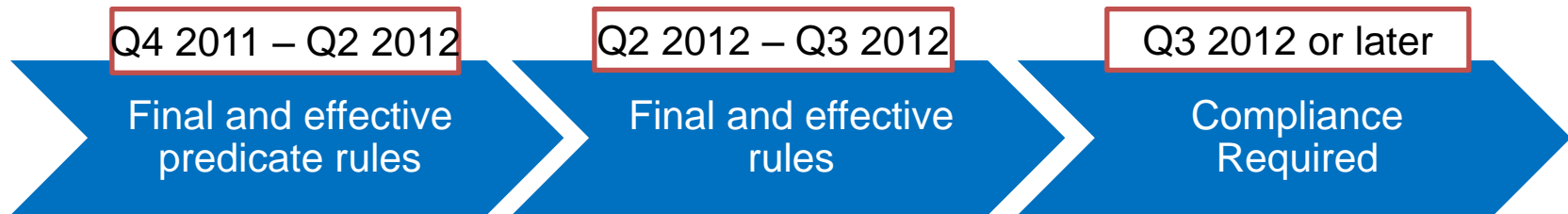
No more execution through voice brokers; consolidation among brokers

Negotiate reporting/clearing arrangements

Will Regional Electricity ISOs become clearing organizations?

Trading Strategies evolve to compress notional values

Compliance Obligations Will be Phased In



- Anti-Manipulation – Final
- Whistleblower – Final
- Position Limits - Final
- Swap Dealer (SD) Definition
- Swap Definition
- SD Registration
- SEF Core Principles
- DCM Core Principles

- Mandated Clearing
- Mandated Trading
- Swaps Documentation
- Margin Requirements

- Within 90 days:
- SDs & MSPs
 - Active Private Funds

- Within 180 days:
- Other Private Funds
 - CPOs

- Within 270 days:
- Third Party Sub Accounts
 - All Others

Key Impact Rules

Conclusions

- Although energy derivatives are a small part of the OTC market, they are covered by the sweeping and comprehensive Dodd-Frank Act
- DFA and its resulting CFTC regulations will impose a significant regulatory burden on energy firms
- DFA will also profoundly and pervasively impact energy markets. Although difficult to predict with precision, some likely consequences will be less hedging, wider bid-ask spreads, and more volatility (a riskier environment)
- DFA will result in increased spend on technology and credit costs, which will lead to increased costs to consumers