



18 January 2021

Electricity Authority
Level 7, ASB Bank Tower
2 Hunter Street
Wellington

To whom it may concern,

Re: Hedge Market Enhancements – Permanent Market Making Backstop

The Electricity Authority ('Authority') is seeking to improve the performance and reliability of market making services in New Zealand electricity futures contracts. The proposal involves permanently implementing the urgent code amendment that was introduced in February 2020.

The Authority is in the process of progressing towards an enduring market making solution. This involves a transition away from the voluntary market making scheme towards a fully commercial market making scheme.

Contact is supportive of the move towards a fully commercial market making scheme. We believe the fully commercial scheme will deliver the most efficient market making outcome for New Zealand electricity market participants and consumers.

After reviewing the proposal, we have concerns with the wording that was used for the urgent code amendment being permanently inserted into the Code, which we outline below.

Open ended mandatory backstop

The Authority identifies that the insertion of the proposed wording would not provide a date of relief for market makers that become subject to the mandatory backstop provision.

Whilst the Authority notes that it will look to reconsider the backstop clause at a later date, Contact strongly recommends that the Authority reconsiders this point, and gives a defined point of relief to a market maker who becomes subject to the backstop.

We believe the Authority should be aiming move as swiftly as possible towards a fully commercial market making scheme, and would like to see incentives placed in the code amendment that result in a defined course of action.

We suggest a number of options that could be considered below.

1. Reinserting the code under an urgent code amendment, such that it would only be valid for 9 months from the date of insertion.
2. Limiting the period which the subpart applies by rewording clause 13.236K(2) such that it reads:

This subpart applies to a participant specified in subclause (1) until 31 January 2022 if that participant:

- (a) is not a party to a NZEF market-making agreement that includes the requirements set out in clause 13.236L; or
 - (b) does not perform market making services in accordance with the NZEF market-making agreement on three or more separate occasions in a period of 90 days, and that non-performance is not permitted by an exemption or otherwise under the NZEF market-making agreement.
3. Limiting the period which the subpart applies to a market maker who is subject to subpart 5 by drafting clause 13.236K(2) such that it reads:

This subpart applies to a participant specified in subclause (1):

- (a) if that participant is not a party to a NZEF market-making agreement that includes the requirements set out in clause 13.236L; or
- (b) for a period of 180 days from the date that the participant has not performed market making services in accordance with the NZEF market making agreement on three or more separate occasions in a period of 90 days, and that non-performance is not permitted by an exemption or otherwise under the NZEF market-making agreement.

Without a date for relief for those market makers who become subject to the mandatory backstop provision, the obligations become significantly more onerous than those made under the urgent code amendment in February 2020, to the point that it relies on the Authority amending or removing subpart 5B for the backstop obligation to be undone.

We recommend that the application of the proposed subpart 5B be limited using one of the three suggestions above.

Relief for third party issues

Contact has experienced a number of occasions where we have failed to meet market making obligations as a result an issue caused by a third party. These incidents have been outside of our control, and have included:

- i. Issues with trading software caused by a fault with the vendor's software.
- ii. Issues with trading orders being rejected due to un-notified changes made to our clearing brokers risk parameters.
- iii. Issues with our clearing broker's maximum order limit being reached, due to all its market makers trying to insert orders within the same one second window.
- iv. Internet connectivity issues.
- v. Fire alarms.

Given the narrow definition of ASX trading platform, we would recommend that the Authority has the discretion to take third party issues into consideration, and relieve the participant of the effects of subpart 5B, if the participant can satisfactorily prove that a third party issue contributed to them failing their market making obligation and bringing subpart 5B into effect.

Minor drafting error

We note there is a minor drafting error in proposed code amendment in Appendix C. Clause 13.236K(2)(c) should be amended to read Clause 13.236K(2)(b).

If there is anything in our response that you wish to discuss further, please feel free to contact me.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'Nigel East', with a stylized flourish extending to the right.

Nigel East
Forward Markets Manager