

9 May 2017

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Submissions
Electricity Authority
PO Box 10041
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Email: submissions@ea.govt.nz

Re: Issues and options paper – Financial Transmission Rights development

Nova Energy (Nova) is pleased to see the wide ranging options being considered for expanding the FTR market. It is our view that creating an active exchange for trading FTRs would be very useful to improving locational risk management in the market. It is also important that FTRs can be paired up with futures contracts, and therefore matching the terms of futures contracts would also be valuable.

Nova also suggests the Authority should consider whether supporting trading of NZ electricity futures on the ASX market is the best option for the New Zealand electricity market. There would be a substantial benefit to New Zealand market participants if they could net off their prudential exposures between physical sales and purchases, CFDs, FTRs, and futures contracts across a single clearing manager. If this cannot be achieved with the current ASX arrangements, then an option of promoting futures trading on a New Zealand exchange should be considered.

If FTRs and futures could be traded in a single market participants would also be able to better match trades to cover locational exposures without the risk of being exposed to partial cover or open positions.

The time that it has taken the ASX to introduce the NZ electricity cap product would suggest that NZ electricity linked products do not carry a high priority in its developments. The current arrangement also creates a dichotomy where NZ resident participants are bound by disclosure rules under the Code, but there is not the same effective jurisdiction over entities based outside New Zealand.

Our detailed response to the questions in the discussion paper is appended to this letter. We would be pleased to have the opportunity to discuss our views further.

Yours sincerely



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Question	Comment
Q1. Do you agree that further enhancing the FTR market could support the issues identified by the Authority, and provide benefits to the wider hedge market?	FTRs have a clearly useful role in enabling retailers, major users and generators manage their exposure to locational price risks. Their usefulness is enhanced if their volumes, location and terms can be matched against futures contracts.
Q2. Are there other issues with the current arrangements for FTRs that we have not identified?	It would be most useful if FTRs and Futures contracts could be transacted on the same exchange and in the same time zone. It would also be very useful if prudential cover could be netted across both exposures as well as against market sales and purchases.
Q3. Are there any other ways to develop the FTR market that we have not identified? If so, please describe them.	
Q4. What are your views on the relative merits or priority of these twelve potential developments? Could some of them complement or substitute for others?	Nova believes that promoting a secondary market for FTRs needs to be given a high priority. This will enable parties to manage locational risk in a more dynamic fashion and to pair up FTRs and futures contracts to provide CFDs to interested parties on wider spread of locations without undue risk.
Q5. Do you agree the Authority should provide policy direction on the four developments in Group 1, but that service providers can lead further assessment of the developments in Group 2?	Nova agrees that service providers could take the lead on the proposed initiatives in group 2. To a degree however, the value of those initiatives to service providers will be enhanced if a platform for secondary trading is successfully introduced. The Authority could still help facilitate developments in Group 2 if it is apparent there is an interest in these, e.g. by preparing standard legal forms that all participants can use to record trades.
Q6. What are your views on the merits of extending direct participation in the FTR market to parties based in Australia?	Nova believes it is unlikely that FTRs sold to Australian parties will be repackaged in any useful form for New Zealand market participants to manage location factors risk. To that extent, the benefits to the New Zealand market of enabling Australian parties to buy FTRs seems limited.
Q7. What are your views on the merits and practicality of allowing parties other than the FTR manager to originate FTRs?	If a secondary market is successfully established then there is no need for third parties to create new FTR's. An alternative is to allow participants to 'borrow' FTRs from parties holding FTRs, in effect, short selling. This could be facilitated by the Authority, e.g. by helping establish standardised legal

Question	Comment
	documentation for trades.
Q8. What are your views on the merits and practicality of developing an FTR derivative product?	We describe an alternative approach below.
Q9. What are your views on the merits of developing a bulletin board?	As stated above, establishing a secondary market for FTRs should be given priority. It is not clear why this should be in the form of a 'bulletin board', and it would seem more appropriate to transact FTRs through an exchange.
Q10. Of the two approaches to overcoming the inherent limitations in the supply of FTRs that have been discussed (allowing parties to originate or develop a derivative product), which do you consider preferable and why?	Nova doesn't believe that either approach is necessary if parties can 'borrow and loan' FTRs.
Q11. Are there other approaches to overcoming the inherent limitations in the supply of FTRs that the Authority has not identified?	Parties can, in effect, create additional FTRs by borrowing units and selling those on the secondary market. The parties lending (1 st) and borrowing (2 nd) can independently determine a fee and prudential and settlement arrangements to cover the risks. The 1 st party in effect preserves their FTR position, but will settle with the 2 nd , borrowing party. The 3 rd party that purchases the FTR from the 2 nd party through the exchange will still settle the FTR through the FTR Clearing Manager.
Q12. What are your views on how these developments would complement each other? To what extent might they be dependent on each other?	