The Electricity Authority - Te Mana Hiko
PO Box 10041
Wellington 6143

9 August 2023

Consultation Paper—Improving Hedge Disclosure Obligations

To whom it may concern,

Thank you for the opportunity to submit on the hedge disclosure obligations consultation.

Bold Trading & emhTrade have been active participants in the New Zealand hedge market for several years, across ASX, FTRs and OTC products. In September 2022, Bold Market Making began providing market making services to the Authority under the first Commercial Making Contract, which has since been renewed until 30 June 2024.

We address the Authority's specific concerns in the requested response form below, but broadly speaking, we are supportive of amending disclosure obligations to capture data related to all OTC transactions. We are aligned with the view that HDO should extend to more nascent contract forms such as PPAs and swaptions and the best way to do so is a blanket disclosure requirement for all OTC trades.

While we believe the hedge market will benefit from disclosure of all OTC transactions, we do not agree the Authority should mandate sharing of full contract documentation.

The proposal to collect all pre-negotiated bid and offer information provides little to no-benefit to the Authority or the market. The costs incurred by individual participants and the regulator are significant, and we predict an unintended consequence of less hedge market liquidity as participants' trade/deal flows are disturbed by onerous record-keeping requirements. If negotiations are subject to enhanced record keeping and therefore carry an increased risk of non-compliance, hedge market trading and participant interactions will suffer.

We welcome any further discussions with the authority and market at large on the points raised below.

Yours faithfully,

Stu Innes
CEO & Co-founder – emhTrade

Georgie Herb
CEO & Co-founder – Bold Trading

Questions	Comment
Q1. Identified Issues	

a. Do you agree with the identified issues? If not, why?	Yes we do generally. Our feedback on each specific point is as follows: **Forward price curve is now available through different sources** We agree the development of ASX futures has reduced the usefulness of some aspects of the HDO over time, particularly as open interest and traded volume has grown and eclipsed OTC. The original motivations for the HDO were to establish a more transparent forward curve and visibility for participants to compare pricing of hedges of a similar nature they may be interested in. Whilst the question of an established forward curve has largely been solved by the ASX, participants will still find that OTC hedge pricing differs greatly after adjusting for numerous other factors. Perceived counterparty creditworthiness, quantity, location and duration of hedges are some variables that skew OTC trade prices. In that sense, the hedge disclosure database still fulfills a very useful purpose for gauging competitiveness of OTC trades. The ASX is limited to two nodes, and 99% of liquidity is in baseload contracts of fixed terms. The standardised nature of futures contracts means the ASX will never be a perfect substitute for OTC disclosure. **The HDO requirements do not accommodate the growing diversity in OTC risk management contracts** Agree. This point raises the question of what contract forms should or shouldn't be captured under HDO. There is an associated difficulty in defining these contract forms and ensuring some degree of future proofing. In our view, requiring disclosure of data related to all OTC transactions is the enduring solution. **Current information on OTC contracts is not sufficient to evaluate market efficiency** ***Term*** The existing 10-year limit on HDO for price & zone has questionable merit in our view. As term increases, so does the opacity of the OTC market and infrequency of trades. This aspect of the contract market is the most fundamental in bringing new entrants, development and innovation to market, and yet it is the most opaque. More transparency in the long-term hedge market will support new generation and retail competition significantly and so the 10-year limit should be abandoned. **The current HDO System delivers poor user-experience and low-quality data**

	We agree. The system is antiquated and adds significant unnecessary friction to the disclosure process. HDO and the HD system must continue to evolve over time, and we encourage the Authority to make changes today that enhance disclosure, and the ability for users to extract insights from the disclosed data. Over time the HDO and system ought to continue to develop, and so periodic reviews to settings and functionality should occur. Too much time has passed since the last review and we believe this can be improved upon.
b. Are there other issues with the HDO requirements that we have not identified? Can you please provide specific and quantifiable examples.	***Options*** The existing disclosure of OTC options has no value, because the strike and premium are not disclosed. The strike is a fundamental characteristic of all option pricing, and without it, participants cannot gather any useful information from the HDO on option pricing. Average rate (Asian) options should be differentiated from those that are a strip of options. ***Non-baseload products*** For any shaped products, the profile should be disclosed and this profile should be made available. We accept that in practice there may need to be some more coarse 'profile' data field than the expected shape in every half hour, however without some information about shape, there is no reliable way of comparing the "peakiness" of such contracts, and therefore the price information is of limited use.
c. What types of risk management contracts are not being captured under the current HDO requirements as set out in the Code?	***Swaption exercise disclosure*** When swaptions are exercised into a swap/CfD, that CfD should be disclosed. It is our observation that there have been inter-generator swaptions that have been exercised into swaps, where the swap leg has not been posted in the hedge disclosure. Under existing code requirements, these CfD legs ought to be captured by the HDO, and we encourage the Authority to review any such instances and remind participants of their obligations. Under current settings, the swaption itself is not required to be disclosed, however any exercise of said swaption that results in a CfD, is separate and distinct from the swaption, and is captured by section 5 of the code.
d. Do you use the published information to elicit a forward price curve and to assess the competitiveness of the contracts market? If not, what do you use it for?	Yes
Q2: Problem definition	

e. Do you agree with the Authority's proposed areas of improvement? If not, why?	Yes
f. Are there other areas of improvement in the HDO requirements that we have not identified?	No
Q3: Improving risk management information collected	

g. What are your views on the relative merits or priority of these five options for improving the risk management information collected? What are the compliance costs?	**(a) collect information on all OTC contracts excluding contracts traded on the ASX** Disclosure of all OTC transactions would enhance transparency and enable increased competition, market efficiency and lead to better outcomes for the consumer. We see this as a worthwhile development, and it should be pursued. The authority's capture of ASX trade data directly from the exchange is sensible and we propose no refinement or addition to this process. **(b) require submission of entire contract** This is of questionable benefit, is unnecessary, carries too much cost and would be too difficult for the Authority to efficiently collect, store and draw comparisons from the information gathered. The bespoke nature and format of OTC contracts and confirmations creates a significant hurdle for the Authority to overcome (in collecting, parsing, storing and utilising the information) and there is no commensurate benefit for the Authority, or market at large. **(c) collect pre-negotiation bids and offers** Strongly disagree. OTC contracts by nature often take long periods of time to negotiate, with dozens of interactions between parties to finalise. While some of the pre-negotiation information can be captured relatively easily, some interactions occur over phone calls and instant messenger applications and are much more difficult to warehouse and share in a useful format. Disclosing all this data will impose significant costs and liability on participants. We note that whilst most participants will have existing processes to record these pre-negotiation interactions, these record keeping systems are designed, primarily, to be used only in the event of a disagreement. They are not designed to be frequently polled, parsed and organised into an all-encompassing data-store suitable for the type of analysis that would generate valuable insights. The data that participants have regarding all pre-negotiation bids/offers/queries etc is generally recovered by 'checking the tapes'. In addition, the Authority would be overwhelmed with information if it were to capture all pre-negotiation interactions. Capturing the information, reformatting it, storing it in a useable format and then drawing conclusions from it would be a significant initial, and ongoing project. Anything is possible, but the cost/benefit of pursuing this work is

	insufficient. The Authority's efforts are better spent in other areas. We applaud the Authority's continued ambition to foster competition and efficient outcomes in the OTC market. Monitoring and engaging with participants that have specific complaints around lack of responses to pricing, when they arise, is the best use of resources in ensuring competitive outcomes. If a participant has a specific complaint, then they need to provide evidence for that. The Authority needs to investigate and then take appropriate action if necessary. For 99% of OTC trades, there is nothing to see and if all such pre-negotiation correspondence was collected, the overwhelming majority would never be assessed. The focus should be on the 1% of trades where there is a perceived or alleged problem. Furthermore, the risk of non-compliance or difficulty in maintaining records will add friction to the hedge market. Consider the likely outcome if representatives of two trading companies only have limited means to communicate at a point in time, perhaps outside of ordinary business hours or due to other technology/location constraints. If these hypothetical traders are limited in the ways in which they can communicate, without fear of breaching information capture requirements, less discussion and ultimately less trading will occur. Countless deals are spawned by cell phone calls, instant messengers or text message. If informal means of communication are hampered by a misguided (albeit well intentioned) regulatory requirement, the proposal will achieve the opposite of its stated intent. Blanket disclosure of all pre-negotiation information will not enhance competition or consumer outcomes and we are opposed to the Authority pursuing this initiative. **(d) remove grid zone areas and require participants to disclose node** We strongly agree with and encourage this development. Disclosure of specific nodes as opposed to the existing grid zone area arrangement would enhance the ability to compare and evaluate relative hedge pricing. Within some grid zone regions there are significant differences in nodal prices, making meaningful comparisons virtually impossible. Moving to nodal disclosure would impose no additional costs on participants (and may even reduce them as there is no intermediate location factor adjustment to make) and will deliver benefits to the market. **(e) require participants to disclose MW as well as MWh** We agree with this initiative and in line with our recommendation above, we would take it a step further and require disclosure of the profile of non-baseload products.

h. Are there any other options to improve risk management information collected that we haven't identified?	Nothing further to add to our options suggested in previous questions.
i. If the Authority were to expand the types of risk management contracts collected: a. What types of contracts should be collected (ie, swaptions, PPA)? b. Should the Authority specify the type of contracts that are required to be disclosed (similar to status quo), or simply amend the Code to capture all existing and any future types of hedge products? Why?	***PPAs*** In our interactions with existing and aspiring renewable developers, questions around available term, pricing and appetite for long term PPAs are by far the most frequent and material to said parties. Uncertainty around pricing and availability of PPAs will be adding friction to the NZ energy development pipeline, if not completely killing some projects all together. There would be a material benefit to New Zealand's development pipeline if PPA hedge prices and terms were disclosed. We appreciate that PPAs are highly bespoke and therefore it is difficult to make apples to apples comparisons between two contracts. However, embedded optionality, price escalators and renewal clauses are examples of material factors that willl influence PPA pricing. If PPAs were to be captured by HDO, one option is to require disclosure of the existence of such parameters (among others). We see this functioning in a similar manner to the existing HDO where certain clauses require disclosure, for example suspension clauses. Commercial sensitivity and confidentiality should be maintained and so we don't believe full PPA agreements need to be shared with the Authority. ***Swaptions*** Swaptions should fall under HDO. We agree all OTC hedge products should be captured. We acknowledge the development required to update the HDO system and the increased costs on participants, but we think the benefit to the wider market and downstream positive impacts to competition and consumer outcomes is a worthwhile tradeoff to make.
j. What risk management information on each type of contracts should be collected, in addition to what is already required under the current Code to support risk management strategies?	We suggest a working group consisting of various parties and participant types should be established to determine what information is material and the costs of collecting/disclosing/reporting such information. Some examples though are: - strike price, and if, for swaptions, this is not fixed, then what inputs are used to set it (ie ASX prices, fuel inputs) - Profile (perhaps through a coarse 144 part profile weighting input) Max / Min volumes (ie take or pay components)
Q4: Improving risk management information published	

k. What are your views on the proposed options? Which one do you think the Authority should adopt when considering what risk management information should be published?	We believe option ***(c): publish a select range of information derived by industry needs***, is the best way forward.
l. Based on the risk management information suggested above (paragraph 4. 8 (a - e)) and any additional suggestions, what risk management information do you think should be published on each type of contracts, and why (or why not)?	Please refer to suggestions above.
Q5: Improving the hedge disclosure system	
m. What improvements do you want to see in the current System, and why? Could you provide specific examples where possible?	Incorporating the new types of contracts outlined in our responses to prior questions would be our only input. It is important that hedge disclosure obligations can be automated. Rather than a simple csv upload, an API would be a vast improvement. This should also extend to querying the site, such that participants can more easily utilise the data available in their own business processes (such as pricing tools or for market analysis). We see the data available as akin to outage or hydrology data. The manual nature of the site is not fit for this purpose.