

vía email: WholesaleConsultation@ea.govt.nz.

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## Improving Hedge Disclosure Obligations (HDO)

Mercury welcomes the opportunity to provide feedback to the Electricity Authority (the Authority) on its consultation paper *Improving Hedge Disclosure Obligations Collection and Publication of Risk Management Information Consultation paper*, 11 July 2023 (Consultation Paper).

The Authority is seeking stakeholder views on options for amending the current HDO requirements to improve the risk management information that is collected and published, as well as improve the hedge disclosure system.

Mercury supports the Authority's decision to update the HDO policy settings with the aim of ensuring that information about the contracts market made available promotes the long-term benefit of consumers. Mercury also supports in general the Authority's assessment of potential options for amending the HDO.

Mercury proposes that for the purpose of collecting, processing and publishing the risk management contract information under the obligation, the Authority should better define categories that capture relevant and comparable contract types. In particular, Mercury considers that the Authority is already collecting information across a wide range of contracts however transparency is being lost with the limited contract types being available to disclose against in the system and as define in the Code.

In addition to updating the Code, Mercury proposes that Authority should engage with industry to develop a common understanding and practice for the implementation of the Code. Initial suggestions for an engagement include the Authority preparing guidelines and/or "cheat sheet", as well as holding industry workshops. Establishing a common understanding and practice will be important for the successful implementation of an updated Code.

Appropriate improvements to the risk management information that is collected and published, as well as improvements to the hedge disclosure system should aim to deepen the contract markets. This should, as the Boston Consulting Group (BCG) report "The Future is Electric"<sup>1</sup> highlights, assist with providing revenue adequacy for flexible resources as well as assisting increased demand side participation.<sup>2</sup>

Mercury expands on these proposals in response to the Authority's questions provided in the annex.

Mercury looks forward to engaging with the Authority and industry stakeholders on further developing, finalizing and implementing the Code amendments.

Yours sincerely,



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<sup>1</sup> BCG report, Climate Change in New Zealand: The Future is Electric, 25 October 2022, page 16.

<sup>2</sup> This recommendation, amongst others proposed by BCG, support its *preferred pathway*, *Smart System Evolution*, page 10.

## Annex: Consultation Paper questions with Mercury's response

Consultation Paper questions	Mercury response
<b>Q1: Identified issues</b>	
a) Do you agree with the identified issues? If not, why?	Mercury agrees with the general scope of the issues identified in the Consultation Paper.
b) Are there other issues with the HDO requirements that we have not identified? Can you please provide specific and quantifiable examples.	Mercury has no further high-level issues to add to those identified in the Consultation Paper.
c) What types of risk management contracts are not being captured under the current HDO requirements as set out in the Code?	<p>Mercury considers that the question should not be about the particular “types” of risk management contracts not being captured, but rather providing better, more clearly scoped definitions of the risk management contract categories.</p> <p>For example, the present “options” contract category in the code is very broad, as it can cover call, put and cap options under a single heading. It may be more appropriate to separate these option types out. However, whether or not separating these option types is appropriate will depend on whether it better promotes the purpose of the disclosure obligations.</p> <p>Similarly, the C300 caps category is very narrow. Whether or not this category should be broadened will also depend on whether it better promotes the purpose of the disclosure obligations.</p> <p>Another example are PPAs, which can be both physically or financially settled.</p> <p>These examples highlight the importance of clearly defining the purpose of the disclosure obligations and particularly how its purpose impacts on the appropriate specification of the contract categories.</p> <p>Mercury therefore proposes that the purpose risk management contracts categories should be defined before relevant categories and data points can be specified.</p>
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?	Mercury uses the published information to gain a better understanding of past transactions in general rather than elicit information about the forward price curve.
<b>Q2: Problem definition</b>	
e) Do you agree with the Authority's proposed areas of improvement? If not, why?	<p>Mercury agrees in general with the Authority's proposed areas of improvement.</p> <p>In addition, Mercury suggests that there are greater gains can be made by focusing efforts on the areas: b) <i>improving the risk management information published</i>; and c) <i>improving the hedge disclosure system</i>. This includes establishing clearly defined contract categories, as discussed above, as well as the operational processes for collecting, processing and publishing data.</p>



Consultation Paper questions	Mercury response
	<p>With respect to area: a) <i>improving the risk management information collected</i>, Mercury suggests that the Authority already collects a substantial proportion of contract information, but that the relevance of this information is obscured by the present specification of contract categories as discussed above.</p>
<p>f) Are there other areas of improvement in the HDO requirements that we have not identified?</p>	<p>Mercury does not consider that there are other general areas of improvement at this point.</p> <p>However, Mercury notes that there are important areas of detail that should be addressed in an updated Code, such as (and not limited to) the definition of trade date. Mercury anticipates that these important details will be addressed in the Authority’s consultation on its preferred options, and communicated in guidelines and industry workshops.</p>
<p><b>Q3: Improving risk management information collected</b></p>	
<p>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?</p>	<p>Mercury supports submitting the complete relevant information and data set required to meet the purpose discussed above. In particular, this includes relevant nodal, MW and MWh information, giving consideration whether it is appropriate to report this information for the relevant category.</p> <p>Mercury, however, requests that the Authority provide more detail regarding the intended purpose and scope of the proposed obligations to: b) <i>require submission of entire contract</i>; and c) <i>collect pre-negotiation bids and offers</i>. It is unclear from the Consultation Paper whether it is envisaged that this is a data and information “dump” or an information request that is more tightly specified, as well as who is expected to provide this information.</p> <p>In either case, Mercury requests that the Authority clarify how it intends to use this information.</p>
<p>h) Are there any other options to improve risk management information collected that we haven’t identified?</p>	<p>Mercury does not consider that there are other general options for improving risk management information collected.</p>
<p>i) If the Authority were to expand the types of risk management contracts collected:</p> <ol style="list-style-type: none"> <li>a. What types of contracts should be collected (ie, swaptions, PPA)?</li> <li>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?</li> </ol>	<p>As discussed above, Mercury considers that the question should not be about the particular “types” of risk management contracts not being captured, but rather providing better, more clearly scoped definitions of the risk management contract categories.</p> <p>As a further example, Mercury understands that the FPVV disclosure requirements in the Code already capture the majority of PPAs. Similarly, swaptions have previously been disclosed as “options”. Therefore, the Authority should have this contract information irrespective of whether the contract type happens to be labeled PPA/FPVV or swaption/option.</p> <p>However, direct supply PPA’s that are applicable to behind-the-meter installations may not be captured by the current obligations. This may require the specification of an additional contract category.</p>



Consultation Paper questions	Mercury response
	To reiterate, Mercury proposes that the purpose risk management contracts categories should be defined before relevant categories and data points can be specified. Providing clarity on products and categories is better than poorly defined contract types
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?	See response to question e, g and i.
<b>Q4: Improving risk management information published</b>	
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?	<p>Mercury supports the option to <i>Publish a selected range of information – derived from industry needs</i>. Appropriately implemented, based on industry input, the published information should promote the long-term benefit of consumers.</p> <p>The option of publishing all OTC contract information, however, raises the risk of disclosing an individual party’s commercially sensitive information, which could harm competition. At the other extreme, publishing no information would result in parties having very little or no information about the state of market on which to base their decisions.</p>
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)?	At this point Mercury has no comment regarding the specific risk management information that should be published as this will depend on the how the contracts are categorized in the Code. The Authority should engage with the industry in order to identify the selected range of information that would meet its needs.
<b>Q5: Improving the hedge disclosure system</b>	
m) What improvements do you want to see in the current System, and why? Could you provide specific examples where possible?	<p>Mercury agrees with the Authority that reducing the compliance burden will be important to creating an effective HDO system. Furthermore, Mercury agrees that the design improvements should include greater use of technology to automate the data collection improve data quality.</p> <p>To facilitate this automation, Mercury proposes that information collection should be standardized and template driven. The specification of the templates should be based on clearly defined specific categories that capture comparable contract types.</p>

