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Electricity Authority  
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## Improving Hedge Disclosure Obligations

Meridian appreciates the opportunity to comment on the Electricity Authority's consultation paper on potential improvements to the hedge disclosure obligations in Part 13 of the Electricity Industry Participation Code.

Meridian has previously supported greater transparency of hedge information, including non-baseload hedge products and bids and offers as well as an update and enhancement to the Electricity Hedge Disclosure System.<sup>1</sup>

In Meridian's opinion the consultation paper could better define the problem that the Authority seeks to address and the objectives or benefits that the Authority seeks to realise through any proposed reforms. In the absence of such a starting point, it is challenging for participants to assess the high-level options presented in the consultation paper.

When the hedge disclosure obligations were first established, the objective was to enable participants to:

- view and compare hedge contract details;
- produce historic contract curves to better understand the market; and
- view historic contracts which may assist when negotiating new hedge contracts.

In Meridian's opinion, those objectives remain valid.

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<sup>1</sup> See submission on MDAG's options paper: <https://www.ea.govt.nz/documents/2539/Meridian.pdf>

The growth of the ASX futures market has enabled more ready access to price curve information for baseload monthly and quarterly products. However, there are potential ongoing benefits if participants are able to access meaningful information about historic contract prices for products that are traded exclusively (or more commonly) on the OTC market, for example, shaped products like peaks and super-peaks. The information currently collected and published by the hedge disclosure system is not sufficient to enable participants to form a view of historic prices for different classes of hedge contract since only the total MWh of any contract is disclosed and the shape is unknown or has to be inferred.

Meridian sees some potential benefits in a system whereby contract information is published or can be filtered by type so participants can see information in respect of, for example:

- retail contracts (FPVV or FPFV);
- baseload contracts for difference;
- peak contracts for difference;
- super-peak contracts for difference;
- options;
- PPAs (potentially differentiated by type, for example generation following wind or solar); or
- other more bespoke contract structures.

The information that would need to be disclosed and published would necessarily vary by contract type in order to provide useful information to participants while still respecting commercial sensitivities and maintaining competitive pressures. The existing information collected and published may be sufficient for retail contracts, baseload contracts, and options. However, more information on MW and relevant trading periods would need to be collected and published to enable meaningful insights in respect of shaped products and PPAs.

We are not aware of any case for changes to the information disclosed and published in respect of retail contracts (FPFV and FPVV). The consultation paper seeks to address issues such as the inability of the current system to capture the growing diversity in *wholesale* OTC contracts. Furthermore, the precursor work by MDAG recommended greater transparency of hedge information because of the increasing importance of contracts as a tool for wholesale buyers and sellers to manage their spot price risk. Meridian doubts whether there would be net benefits in changing the information collected and disclosed in respect of retail contracts given the lack of identified problem and the high costs to, for example, reduce the volume thresholds for disclosure or to disclose information on all bids and offers for retail contracts.

In a similar fashion, the existing obligations in respect of options may be sufficient. The price of options is not currently published because there are so many possible value trade-offs between strike price and option premium, which makes constructing a reference price curve very difficult.

The same challenges will arise in respect of swaptions given the potential value trade-offs between various terms and conditions of swaptions including:

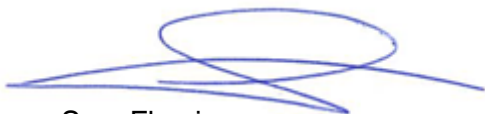
- price;
- force majeure terms;
- times available;
- GWh available;
- location;
- trigger conditions; and
- flexibility of call – in terms of both notice requirements and minimum durations.

Again, this would make it difficult to establish any meaningful reference price curve. Larger swaptions also tend to be bespoke and highly tailored to the risk management requirements of the parties so any sort of reference curve will likely be meaningless to others for negotiation purposes and not useful as a price indicator for other contracts.

In any subsequent rounds of consultation, we would hope to see more detailed information from the Authority on what purpose it wants to achieve with hedge disclosures and more fulsome descriptions of the options so that participants can meaningfully engage. The costs and benefits of any preferred options should also be thoroughly tested.

Meridian's responses to the consultation questions are appended.

Nāku noa, nā



Sam Fleming

**Manager, Regulatory and Government Relations**

## Appendix A: Responses to consultation questions

| Q1. | Identified issues  |  |
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| a.  | Do you agree with the identified issues? If not, why?  | <p>The emergence of a forward price curve for contracts traded on the ASX is not an <i>issue</i> it is another source of information for participants.</p> <p>Meridian agrees that the current hedge disclosure requirements do not accommodate the growing diversity in risk management contracts.</p> <p>We agree that the Authority should have access to information to enable market monitoring, evaluate market efficiency, and inform regulatory decisions. However, it is not clear what information the Authority needs to enable this. The Authority should be clear what the purpose of its monitoring is and assess whether any benefits of improved monitoring outweigh the costs to participants of providing information. The burden of information provision to the Authority has grown significantly in recent years and the Authority seems inclined to seek ever increasing information with limited regard for costs, including the aggregate burden of various reporting regimes across different workstreams. From a participant perspective, there is no feedback or visibility of whether the information is useful or delivering any insights.</p> <p>We agree the hedge disclosure system is dated and there may be improvements that could be made to increase usability. However, we have systems in place to process bulk uploads via .csv files and it is not immediately clear to us what would improve the user experience. Other changes to the platform will depend on any changes to the underlying disclosure obligations.</p> |
| b.  | Are there other issues with the HDO requirements that we have not identified? Can you please provide specific and quantifiable examples. | No.  |
| c.  | What types of risk management contracts are not being captured under the current HDO requirements as set out in the Code?                | <p>The consultation paper states that “long-term renewable energy contracts such as Power Purchase Agreements (PPAs), shaped products and Swaptions are not captured under the current Code requirements.” In Meridian’s opinion, this is not necessarily the case. For example:</p> <ul style="list-style-type: none"> <li>• The Code defines contract for differences broadly such that it would also capture shaped products, for example peak and super-peak</li> </ul>  |

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|     |   | <p>hedge contracts are also contracts for difference.</p> <ul style="list-style-type: none"> <li>• PPAs are generally contracts for difference albeit with long terms and variable volumes matched to physical output from new generation.</li> <li>• Swaptions may be a type of option contract as that term is defined in the Code.</li> </ul> <p>The issue is not so much that these types of contracts are not captured but rather that they are not captured in a useful way. For example:</p> <ul style="list-style-type: none"> <li>• Prices need not be disclosed for contracts for difference with a term less than ten years, whereas most PPAs will have a longer term and it will be challenging to disclose a quantity in MWh of electricity to which the contract relates if the quantity is linked to variable output from a generating station.</li> <li>• It is not clear when a price is for a peak or super-peak contract because all that must be disclosed is the fact that the contract does not apply to all trading periods and a total volume in MWh.</li> <li>• In general, the more bespoke the contract terms the less likely it is that the hedge disclosure information will be useful to other participants.</li> </ul> |
| 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? | Meridian occasionally uses the information published on the hedge disclosure system. For example, if we miss out on a competitive tender process, we might look to see if we can identify whether a similar contract was transacted and at what price to see how far out of contention we were.  |
| Q2. | Problem definition  |  |
| e.  | Do you agree with the Authority's proposed areas of improvement? If not, why?   | <p>It seems logical to consider three separate areas for improvement:</p> <ul style="list-style-type: none"> <li>• the risk management information <u>collected</u>;</li> <li>• the risk management information <u>published</u>; and</li> <li>• the hedge disclosure <u>system</u>.</li> </ul> <p>However, this is not a problem definition. A robust problem definition or objective will be critical to the success of any reforms. It is not clear from the consultation paper what problem the Authority wants to address or what the objective of any reform would be.</p> <p>When the hedge disclosure obligations were first established, the objective was to enable participants to:</p> <ul style="list-style-type: none"> <li>• view and compare hedge contract details;</li> </ul>  |

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|     |  | <ul style="list-style-type: none"> <li>produce historic contract curves to better understand the market; and</li> <li>view historic contracts which may assist when negotiating new hedge contracts.</li> </ul> <p>In Meridian’s opinion, those objectives remain valid and the problem that now arises is that the information collected and disclosed is not sufficient to enable an understanding of or comparison of hedge contracts of different kinds or to enable participants to form a view of historic prices for different classes of hedge contract. Being able to do this may result in benefits, particularly for the types of contracts more commonly traded in the OTC market rather than ASX and for which there is therefore more limited price curve information available.</p>   |
| f.  | Are there other areas of improvement in the HDO requirements that we have not identified?  | Not that Meridian has identified at this stage.  |
| 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? | <p>Meridian would prioritize collecting information on:</p> <ul style="list-style-type: none"> <li>All OTC contracts, with the potential exception of Exchanges for Physical since disclosure of these contracts would not tell the Authority or participants anything useful – there is no change in risk position, only a change in the platform used for the transaction which would be priced at ASX prices and using an equivalent structure, meaning the ASX forward curve will already be the best reference point for participants.</li> <li>Requiring participants to provide information on MW as well as MWh and also the trading periods to which the contract applies – this is necessary in order to usefully distinguish between different shaped products and enable comparison of contracts with similar characteristics, i.e. comparing prices for peak hedges (rather than comparing baseload, peak, super-peak and other shaped contracts with limited ability to understand the differences and what might drive price variability).</li> </ul> <p>We can see why collecting information on bids and offers (as well as transacted contracts) might be useful for the Authority’s monitoring of the OTC market. However, because bids and offers are not actually transacted they contain little, if any, information of value to participants. If the Authority decides to progress information collection on bids and offers, it should be mindful of the cost burden on participants and take steps to minimize costs including:</p> |

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|    |   | <ul style="list-style-type: none"> <li>• consider the most administratively efficient way to collect the information – in Meridian’s opinion this would mean making the parties issuing RFPs or RFIs or initiating a negotiation responsible for submitting information rather than all respondents in those processes;</li> <li>• consider limiting the information collected to only bids or offers capable of acceptance rather than any tentative conversations early in a negotiation; and</li> <li>• consider excluding bids and offers for retail contracts (FPVV and FPFV) as the purpose here seems to be more about monitoring the OTC wholesale market for hedges – see further comments on this point in the body of this submission.</li> </ul> |
| h. | Are there any other options to improve risk management information collected that we haven’t identified?  | Not that Meridian has identified at this stage.  |
| i. | <p>If the Authority were to expand the types of risk management contracts collected:</p> <ul style="list-style-type: none"> <li>• What types of contracts should be collected (ie, swaptions, PPA)?</li> <li>• 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> </ul> | Information on risk management contracts of all types should be collected and the obligation should refer to broadly defined hedge or risk management contracts rather than trying to list all currently known and potential future contract structures.   |
| 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?   | Aside from information to support the Authority’s monitoring function, the information that should be collected will be linked to the information that should be published and the underlying purpose of such publication.   |

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| Q4. | Improving risk management information published  |  |
| k.  | <p>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>   | <p>There is so little information in the consultation paper that it is difficult to comment in a meaningful way.</p> <p>Publishing <i>no</i> information or publishing <i>all</i> information do not seem like realistic options.</p> <p>In Meridian's opinion there may be benefits (over and above the status quo) from publishing a select range of information derived by industry needs. However, before we could comment further, the Authority would need to present far more information about how this could work and how to strike the right balance between the benefits of informed market participants and the costs if commercially sensitive information is published and/or there are effects on competition.</p>  |
| l.  | <p>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)?</p> | <p>Information that is relevant to the valuation of the contract and may be beneficial to participants will vary by contract type and structure. As already mentioned, information about the MW and trading periods covered by a contract will be relevant to understanding the value of different shaped products.</p> <p>For PPAs it may be useful to understand the type of generation that it is linked to e.g. solar or wind to understand the expected shape and underlying price drivers.</p> <p>See also our comments in the body of this paper on the challenges associated with publishing meaningful price information for options and swaptions.</p> <p>Risk management information could be published in such a way that grouping and comparison by contract type or share is possible.</p> <p>In Meridian's opinion, while it may be useful for the Authority's monitoring if it has access to information about grid node and parties to a contract, in terms of what information is published, anonymization by grid zone remains necessary to protect the identities of large industrial counterparties and the effective prices paid by those parties for energy. MEUG members will be better placed to comment but there is likely to be commercial prejudice to those parties if their energy costs are public as it will affect their ability to effectively negotiate contracts in future.</p> |
| Q5. | Improving the hedge disclosure system  |  |
| m.  | <p>What improvements do you want to see in the current System, and why?</p>  | <p>At this time, we have not identified any obvious improvements that could be made to the user experience. We have existing systems in place to use the bulk upload facility with .csv files.</p>   |