



# MAJOR ELECTRICITY USERS' GROUP

10 March 2008

Caroline Ramsey  
Manager Financial Sector  
Competition, Trade & Investment Branch  
Ministry of Economic Development  
By email to [caroline.ramsey@med.govt.nz](mailto:caroline.ramsey@med.govt.nz)

Dear Caroline

## **Submission on draft Emissions Units, Settlement Systems and Futures Bill**

1. This is a submission by the Major Electricity Users' Group (MEUG) on the Ministry of Economic Development discussion paper *Consultation on the Draft Emissions Units, Settlement Systems and Futures Bill*, published 11<sup>th</sup> February 2008.
2. MEUG supports a legislative framework for financial markets that enables competition and innovation. The interest of MEUG and its members in this discussion paper is the effect on arrangements (bi-lateral, OTC, through to competing clearing houses for future instruments) for managing electricity cost risk and rights and obligations for physical emission units. The legislative framework needs to be permissive and enabling to allow the financial markets, physical markets and participants in both to make arrangements that suit their needs.
3. MEUG submits:
  - a) Serious concern at the perception that Cabinet was "captured" by NZX wishing to promote their particular business model. The paper from the Minister of Commerce to Cabinet Policy Committee titled<sup>1</sup> "*Reform of the law relating to futures exchanges and clearing and settlement systems*" (POL (07) 382) of October 2007 sets out in detail the wishes of NZX. NZX was the only non-government or regulatory agency consulted in the preparation of the paper<sup>2</sup>. The Minister proposed only consulting NZX on the outcome of Cabinet's decision even though competing platform providers would be affected<sup>3</sup>.
  - b) The policy issues of improving the efficiency of New Zealand's financial markets in general and clarity on Emissions Units need to be considered separately. Making this separation will assist consideration of the proposals and reduce concerns of any ongoing "capture" noted above. The main risk of confusion is because the generic changes to improving New Zealand's financial markets involve risk management instruments whereas the Emission Units policy issues relate to a physical compliance market.

Recommendation 25<sup>4</sup> of the Ministers Cabinet paper of October did make this distinction, however the Regulatory Impact Statement (RIS) bundled the policy issues and options.

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<sup>1</sup> Refer [http://www.med.govt.nz/upload/53676/POL-\(07\)-382.pdf](http://www.med.govt.nz/upload/53676/POL-(07)-382.pdf)

<sup>2</sup> Ibid, paragraph 82.

<sup>3</sup> Ibid, paragraph 90.

<sup>4</sup> Ibid, paragraph 91, recommendation 25, p18

- c) On the generic changes to settlement systems and futures:
- i) It is not clear how a designated settlement system would work for existing large end consumers with negative pledge obligations with trading banks.
  - ii) When considering a request for a party to be a designated settlement system, MEUG suggest the joint regulators:
    - Be obliged to consult on that request before making a decision, ie additional requirement under s156X (2); and
    - Can set conditions for accepting an application, ie additional clause under s156Y (1) to allow discretion, not just a yes or no decision.
  - iii) A second discussion paper be prepared and consulted on taking into account comments from this first round. The second discussion paper should have a draft RIS examining only the impact of the generic changes, ie excluding policy changes relating to Emission Units. This should include some evidence of the comment in the RIS attached to the Ministers paper of October 2007 of<sup>5</sup>:
 

“A perception that the New Zealand regulatory environment does not conform with international best practice ...”

If this perception is strong and evidence that, for example, futures markets in New Zealand have suffered, then that assists justify these changes. If not, then there should be less urgency to make some of the generic changes.
- d) On the proposed changes relating to Emission Units:
- i) The paper recognises Emission Units are not financial risk management instruments or “securities.” MEUG agrees. Emissions Units are traded in various ways including physical forward transactions. The Bill isn't clear that these types of transactions are also not “securities.” MEUG suggest the Bill needs to be more explicit on this point.
  - ii) A second discussion paper be prepared and consulted on taking into account comments from this first round. The second discussion paper should have a draft RIS examining only the impact of the policies compared with other policy options for a range of scenarios.
 

For example the discussion paper and Cabinet papers in several instances suggest Emission Units are or will be predominately traded through exchanges. This could be termed the traded exchange scenario. MEUG disagrees. Emission Units in Kyoto compliant and non-Kyoto compliant units internationally and in New Zealand are largely traded bi-laterally or OTC. We expect this will continue to be the case in the near term. This could be termed the status quo scenario. The RIS is silent on which of these scenarios is the counterfactual; possibly because the RIS covers both emissions units and generic changes. Unbundling this analysis and more accurate specification of the counterfactual and scenarios we think would better inform the debate and create confidence and support for any final proposed changes.

4. This submission is not confidential.

Yours sincerely



Ralph Matthes  
Executive Director

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<sup>5</sup> Ibid, RIS, p19