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Submission on Reforming the NZ ETS - Rules for Auctioning

Introduction

1. This is Vector Limited's (Vector) submission on the Ministry for the Environment's (MfE) technical consultation document, *Reforming the New Zealand Emissions Trading Scheme: Rules for auctioning*, published in November 2019.
2. Vector supports the introduction of auctions under the New Zealand Emissions Trading Scheme (NZ ETS) as a tool for reducing emissions and enabling New Zealand to more efficiently and effectively meet its climate change objectives. Auctioning would help align the supply of NZUs with New Zealand's emissions reduction targets and provide certainty to NZ ETS participants and the wider economy.
3. The use of the auctioning mechanism would enable entities across the economy to make informed decisions on how they can best reduce their emission levels. This includes innovating and investing in new technology solutions that use renewable energy which Vector, as a leading technology solutions company with a vision of *creating a new energy future*, is well placed to promote and enable.
4. We set out below our responses to selected questions in the technical consultation document. We also suggest a few improvements to the proposed auction rules.
5. No part of this submission is confidential. Vector's contact person for this submission is:

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Responses to selected technical consultation questions

Q1: Do you agree that auction volumes should be evenly distributed over the calendar year?

6. Yes, we agree that auction volumes should be evenly distributed over the calendar year.

Q3: Do you think that unsold units should be:

- All added to the next auction
- Added to subsequent auctions within a limit (preferred)
- Other, please specify.

7. We agree with MfE's preferred option, which is to add unsold units to subsequent auctions within a limit.

Q6: The surrender date in the NZ ETS is 31 May. How far in advance of this date should the closest auction be scheduled? Please consider both monthly and quarterly auction scenarios.

8. We prefer that the closest auction be scheduled a month ahead of the surrender date in the NZ ETS of 31 May and other 'key periods', e.g. Easter, Christmas and New Year's holidays.

Q8: When a price trigger is reached in the cost containment reserve, how should the volume of units from the reserve be sold?

9. The units from the cost containment reserve should be added to the auction volume when a trigger price is reached, with the floor set at the level of the trigger price. We would have concerns if a further auction is held for the sale of the cost containment reserve where a different set of rules will apply, e.g. limitations on which parties could participate. This could create distortions in the clearing price across the original auction and the auction for the cost containment reserve.

Q10: Do you agree that the cost containment reserve should have a single price trigger for all the reserve volume?

10. Yes, the cost containment reserve should have a single price trigger for all the reserve volume to avoid complexity.

Q11: How far in advance should the auction notice be published?

- 60 calendar days (only an option if auctions held quarterly)
- 30 calendar days
- Other, please specify.

11. Our preference is for the auction notice or schedule of the next auction to be announced at the same time as the auction results for the previous auction are published.

Q12: Do you have any comments on the pre-registration process?

12. In our view, a higher level of collateral should provide sufficient protection against non-payment and other financial risks. This would allow interested entities to avoid the multiple requirements associated with the 'intention to bid' form and encourage greater participation in auctions.
13. We suggest a bank account type of arrangement where bidders' account/fund would contain 100 per cent of the value of their bids.

Q13: Do you agree that an intention to bid form must be submitted a minimum of 28 calendar days in advance of an auction?

14. We do not believe it is necessary for an interested entity to submit an intention to bid form at least 28 calendar days in advance of an auction if that party's collateral levels are sufficient. This would simplify the application process, lower transaction costs for interested entities, and encourage greater participation in the auctioning process by removing a potentially unnecessary process.

Q14: Do you agree that bidders should have to provide collateral to participate in an auction?

- Yes
- No
- Unsure.

15. Yes, we agree that bidders should have to provide collateral to participate in an auction.

Q15: If collateral is required, how much should it be?

- Between 10 and 25 per cent of the maximum bid value (preferred)
- 100 per cent of the maximum bid value
- A flat rate payment, please specify amount
- Other, please specify.

16. As indicated in our response to Q12, our preference is for 100 per cent of the maximum bid value to be required as collateral. This would allow an entity to bid only when its money is 'locked' in that entity's account.

Q16: What forms of collateral should be accepted?

- Cash
- Bank guarantee
- Irrevocable letter of credit
- Credit rating (not preferred)
- Other, please specify.

17. Cash and bank guarantee are our preferred options.

18. There are several examples of entities operating trading platforms that manage the issue of payment default that MfE may gain insights from. One such example is emsTradePoint.

Q17: How many days before an auction do you think is sufficient lead time for provision of collateral (Government suggests five business days)?

19. As indicated in our response to Q16, a bank guarantee/account type of arrangement is one of our preferred options for simplicity reasons. This would allow an interested entity to avoid 'repeating' the process of providing collateral for future auctions that entity intends to participate in.

Q18: Do you agree that collateral (depending on its form) should be used against payments for successful bids, if the bidder requests?

- Yes
- No
- Unsure.

20. If the collateral held is in cash form, that collateral should be used against payments for successful bids.

21. If the collateral held is in the form of a bank guarantee, then a payment request should be made, with payment to be made within a set number of days.

Q19: Do you agree that bidders should be able to choose to have their collateral automatically returned, released at their request, or retained for future actions?

- Yes
- No
- Unsure.

22. Yes, we agree that bidders should be able to choose to have their collateral automatically returned, released at their request, or retained for future actions. However, the entity should only be able to submit a bid for a tender so long as collateral is in place at the time the bid is submitted. That entity should only be able to withdraw or release collateral to the extent that it is not required to support 100 per cent of a current bid.

Q20: What should be the minimum number of NZUs that can be sold at auctions?

- 100 NZUs
- 500 NZUs (preferred)
- 1000 NZUs
- Other, please specify.

23. We agree with MfE's preferred option of setting the minimum number that can be sold at auctions at 500 NZUs, with no limits to unit increments and price.

Q21: Bids are only accepted in multiples of minimum lot size. What should the minimum lot size be for auctions?

- 100 NZUs
- 500 NZUs (preferred)
- 1000 NZUs
- Other, please specify.

24. Our preference is for bids to be accepted in multiples of a minimum lot size of 100 NZUs. This would incentivise greater participation in auctions and provide more flexibility for bidders. Where an electronic platform/process is in place, there does not seem to be any value in having a higher lot size.

Q22: What should the minimum price increment be?

- \$0.01 - \$0.02
- \$0.05 (preferred)
- \$0.10
- Other, please specify.

25. Our preferred price increment is \$0.01 to provide the greatest flexibility for bidders. We do not consider this to be challenging to implement with an electronic platform/process.

Q23: Do you think a maximum bid limit should be set?

- Yes
- No
- Unsure.

26. Yes, a maximum bid limit should be set to manage the potential risk of one entity "dominating the market by purchasing a large number of units and using this to their advantage". Analysis would need to be done to determine the appropriate maximum bid limit.

Q26: How do you think tied bids should be resolved?

- Random assignment to the entire bid
- Random assignment by lot (preferred)
- On a pro-rata basis, with rounding
- Other, please specify.

27. We agree with MfE's preferred option to randomly assign tied bids by lot.

Q27: Do you agree that a technical reserve price should be set for auctions?

- Yes
- No
- Unsure.

28. Yes, we agree that a technical reserve price should be set for auctions.

Q28: If a technical reserve price is set, do you agree that the methodology for calculating the price be kept confidential?

- Yes
- No
- Unsure.

29. Yes, we agree that the methodology for calculating the price be kept confidential for the reasons stated in the technical consultation document.

Q29: What results should the auction operator publish as soon as practicable following an auction? Please select all that apply.

- Clearing price
- Total volume of units auctioned
- Total volume of bids
- Average bid size
- Number of bids
- Cover ratio (total volumes bid divided by total volumes for sale)
- Total number of bidders and the number of successful bidders
- Number of unsold units, if any
- Other, please specify.

30. All of the above should be published by the auction operator as soon as practicable following an auction. As proposed in our response to Q11, the next auction date should also be announced/published at the same time.

Q30: What is the best approach for settlement of successful bids?

- Payment before delivery (preferred)
- Delivery versus payment
- Other, please specify.

31. We suggest the adoption of a 'payment on the day' approach for the settlement of successful bids.

Q31: Do you have a view on the time for settlement (suggested it may take 4 business days)?

32. We suggest that settlement should be no later than 3 business days, assuming all transactions will be in automated or electronic form.

Q32: What information should the auction monitor report include? Please select all that apply.

- Detailed volume statistics (e.g. average volume bid per bidder)
- Detailed statistics on number of bids (e.g. average number of bids per bidder, number of bids submitted, number of successful bids)
- Relevant aggregate information (e.g. largest bids as percentage of total volumes sold, percent of volumes awarded to entities with mandatory obligations)
- Relevant distributional information (e.g. number of units awarded to which winner, with bidder names withheld)
- Distribution of successful bids among market participants with and without mandatory compliance obligations
- Relevant information to resolve tied bids
- Other, please specify.

33. All of the above information should be published by the auction monitor together with any recommended improvements to the auction process/system.

Q33: Do you think that releasing information on the number of NZUs won by each successful bidder, who will not be named, would raise any issues of data confidentiality?

34. No, we do not believe that releasing information on the number of NZUs won by each successful bidder, who will not be named, would raise any issues of data confidentiality.

Q34: Does auction monitoring reporting raise any concerns for you with respect to commercially sensitive information?

35. No, we do not believe auction monitoring reporting will raise issues with respect to commercially sensitive information - from our perspective.

Q35: How often do you think the auction monitor should review the auctioning system?

- After one year initially, then every two years thereafter (preferred)
- Annually
- Other, please specify.

36. The auction monitor should review the auctioning system a year after the first auction, then every two years thereafter, which is MfE's preferred option.

Q36: Do you have any other comments?

37. To promote transparency and instil confidence in the auction system, we suggest that the auction operator and the auction monitor be selected through a contestable process.

Concluding comment

38. We are happy to discuss any aspects of this submission with MfE officials.

Yours sincerely
For and on behalf of Vector Limited



Richard Sharp
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