Inefficient Price Discrimination in very large electricity contracts

Code Amendment

Decision paper

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Executive Summary

Decision

1.1 The Authority has decided to make a permanent amendment to the Electricity Industry Participation Code 2010 (Code) (Code amendment) to address the potential for inefficient price discrimination in very large contracts. The Authority's decision follows an extensive consultation process - the Authority consulted on the issue of inefficient price discrimination and possible policy solutions in the *Inefficient price discrimination in the Wholesale Electricity Market – Issues and Options Discussion* Paper in October 2021 and consulted on a proposed Code amendment in August 2022. This permanent Code amendment will replace the existing urgent Code amendment that was introduced in August 2022.

1.2 The Code amendment prohibits generators giving effect to materially large contracts (MLCs) unless the net value from the contract is positive relative to alternatives *or* the buyer can on-sell un-used electricity under the MLC on no worse terms than if they had consumed the electricity themselves. The Code amendment also provides the Authority with greater visibility of MLC contracts for the purposes of monitoring and compliance through the disclosure obligations. A voluntary clearance process is set out in the Code amendment which gives generators the option to gain assurance that the MLC is not in breach of the Code amendment and that the Authority will not investigate a contract at a later date.

Rationale for decision

1.3 The Issues and Options paper highlighted the incentives generators may have to subsidise extremely large load customers that could otherwise credibly exit, reduce consumption, not expand or not enter the domestic market. This incentive arises from the increase in aggregate demand, arising from the large user's consumption, inflating electricity prices nationally to such an extent that the higher revenues generators earn from all other (inframarginal) consumers greatly exceeds the cost of the subsidy required to retain the large load user. In effect, generators could withhold supply to consumers by supplying electricity to a large load user that would otherwise have exited (or not entered the market) if they faced the true direct value of that electricity. Such arrangements may result in large efficiency losses and wealth transfers from consumers to all generators.

1.4 The Authority is of the view that generators may have on-going incentives to enter, modify, or extend inefficient arrangements with respect to contracts:

(a) which involve a 'credible threat to consumption' – that is, they relate to a customer likely to otherwise exit or not enter the market (ie, not be attracted to locate domestically) or a customer who otherwise would reduce or not expand consumption;

(b) where the contract price is conditional on the consumption of a quantum of electricity by the designated large load user; and

(c) where the quantum of electricity involved is sufficiently large to materially increase prices being faced by other consumers (ie, that are not party to the arrangement).

1.5 Contracts with the potential to satisfy these conditions are very low in number – perhaps no more than two or three contracts each decade. However, they each are significant in terms of the share of national generation they allocate and the potential for severe adverse impacts on consumer outcomes where they are inefficient. There are indications that a number of negotiations over consumption arrangements which meet these conditions will occur in the near to medium term. Examples include a possible new, modified or extended electricity contract for the New Zealand Aluminium Smelter (NZAS) in advance of the conclusion of the current contract in 2024, and negotiations arising through the market development efforts of generators, most notably Meridian and Contact,

to attract large load users such as a hydrogen plant and data centres to the lower South Island.

1.6 The Authority is of the view that the Code amendment is in the long-term interests of consumers as it will mitigate potentially very significant efficiency losses and wealth transfers associated with these arrangements.

The Code amendment

1.7 After considering feedback on the consultation paper the Authority has decided to make minor amendments to the proposed Code amendment to better reflect the Authority's policy intent. These amendments largely relate to:

(a) the definition of materially large contracts (13.268(1)(a))

(b) how the Code applies to two or more contracts which may together create the conditions for inefficient price discrimination (13.268(1) (b) and (c))

(c) clarifying that netting of new generation is allowed where the material large contract is "material" to the generator's decision to invest in the new generation (13.268(4))

(d) refinements to the scope of the disclosure requirements (deleted 13.271(2)(d))

(e) disclosure obligations and potential non-application of a clearance in cases where there are delays or changes to forecast new generation (13.271(1) and 13.273(6))

(f) transitional arrangements relating to applications made under the urgent Code (13.282)

1.8 The effect of these changes is to ensure the Code amendment does not create unnecessary and disproportionate barriers or uncertainty, including with respect to very large contracts linked to investment in new generation. In upcoming years, a significant amount of investment is needed to transition to 100% renewables. The Authority has designed the Code amendment to exempt quantities of electricity from the net 150 MW threshold sourced from contracts such as power purchase agreements (PPAs) which support the transition, to the extent that they are material to the MLC and result in improved supply of generation. The Code amendment only applies to generation used to supply a large load user which would otherwise be used to supply the rest of New Zealand in the absence of the contract.

1.9 The Code amendment revokes the urgent Code and is inserted into Part 13, subpart 7. The Code amendment:

(a) applies to 'materially large contracts' (MLCs), being contracts (or combinations of contracts) not entered into through a derivatives exchange and includes terms under which the buyer itself will consume a quantity of electricity of net 150MW or more.

(b) prohibits generators from giving effect to MLCs unless:

(i) the net value of the MLC is positive – ie, the direct value to the generator of the contract exceeds the value of the generator's best alternative, or

(ii) the contract allows the large load user (buyer) to on-sell all un-used electricity under the contract without the load user being subject to any worse terms than if it had consumed the relevant quantity itself, or

(iii) the Authority has provided clearance of the MLC (see below) and that clearance remains effective and applicable.

(c) requires generators to disclose new or modified MLCs to the Authority as well as supporting information e.g. the rationale underpinning pricing or the implications of resale conditions.

(d) introduces a voluntary clearance regime which gives generators the option to de-risk contracts by obtaining clearance of draft contracts or signed contracts that are conditional on clearance. If a contract is cleared (and that clearance remains effective and applicable), then the MLC is exempt from the prohibition at (b) above.

1.10 If a generator opts for voluntary clearance, it must provide the Authority with the proposed unsigned contract, or a contract which is conditional on clearance and the same supporting information as required under the disclosure regime (under (c) above) to allow the Authority to determine whether it is eligible for clearance (based on the Authority being satisfied as to either (b)(i) or (ii) above). The Authority generally has 45 business days to make its decision, and a generator needs to enter the contract within 20 business days of clearance (where the contract was provided un-signed), otherwise clearance lapses. The clearance remains effective and applicable unless key aspects of the contract are changed post-clearance, or the information provided by the generator in support of the clearance is later shown to be false or misleading.

What this decision paper does

1.11 This decision paper:

(a) Summarises the Authority's response to submissions received on the proposed Code amendment *"Inefficient Price Discrimination in very large contracts – Consultation Paper"* between 18 August-31 October 2022

(b) Sets out the Authority's decision and the finalised Code Amendment, including revocation of the urgent Code and transitional arrangements should any clearance applications be received prior to revocation.

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2. The Authority has decided to require disclosure of and provide a voluntary clearance regime for very large contracts with the potential for inefficient price discrimination

2.1. Having considered the submissions in response to the consultation paper *Inefficient Price Discrimination in very large electricity contracts* the Authority has determined to introduce permanent Code (to replace the current urgent Code) to address the potential for inefficient price discrimination in very large contracts which can or may move market prices nationally.

2.2. The Code defines Materially Large Contracts (MLCs) - which are contracts (or combinations of contracts) not entered into through a derivatives exchange and includes terms under which the buyer itself will consume a quantity of electricity of net 150MW or more at a point in time. The Code also imposes restrictions on giving effect to these contracts. The Code includes provisions to combine two or more contracts in specific circumstances for the purposes of determining whether in combination the contracts constitute a MLC.

2.3. The Code prohibits generators from giving effect to MLCs unless:

(a) the generator can demonstrate that the net value of the MLC to the generator is positive, consistent with the provisions setting out the calculation of net value; or

(b) the generator can demonstrate that the buyer is allowed to on-sell all unused MW without the buyer being subject to any worse terms than if the buyer had consumed this electricity itself; or

(c) having received an application from the generator, the Authority provides a clearance for the MLC.

2.4. The Code also provides for the disclosure of information related to all MLCs by the generator to the Authority, when seeking a clearance or entering or making significant changes to a MLC.

3. The Code amendment will provide long-term benefit to consumers

3.1. The Authority is satisfied that in some situations generators may face incentives to subsidise large load customers that could otherwise credibly exit, reduce consumption, not expand or not enter the domestic market. This potential incentive arises from the increase in aggregate demand, arising from the large user's consumption, inflating electricity prices nationally to such an extent that the higher revenues generators earn from all other (inframarginal) consumers greatly exceeds the cost of the subsidy required to retain the large load user. The potential incentive is that generators effectively withhold supply to consumers by supplying electricity to a large load user that would otherwise have exited (or not entered the market) if they had faced the true direct value of that electricity. Such arrangements can be characterised as rent seeking – a situation where an entity seeks to capture more wealth for itself without adding to, and potentially while destroying, wealth to society - by way of a sophisticated form of economic withholding.

3.2. The Authority's concern is not per se with prices rising due to a large load user's consumption decisions. Price responses to legitimate changes in supply and demand conditions and expectations is the underpinning of an efficient market system, with prices serving as a credible signal to inform consumption, dispatch and investment decisions. Nor does the Authority object to price discrimination per se - selling at different prices to different consumers can increase wealth to society through expanding the number of consumers served.

3.3. However, the focus should be on facilitating price discrimination, which is efficient, and deterring price discrimination which is not in the long-term interests of consumers.

Moreover, the Authority's concern is specific to the case where prices rise for other consumers because of a large load user's decision to consume more than they otherwise would be due to generators' incentives to offer them access to electricity at a subsidised rate. Subsidising large load customers in this way creates the possibility that electricity is not being allocated efficiently. If the resulting increases in spot and forward prices can be sustained due to generators exercising market power without inducing entry, this distorts investment and electrification signals, and enables a wealth transfer from all other consumers to generators. This is unlikely to be in the long-term interests of consumers.

3.4. Having considered submissions on the proposed Code amendment and made some amendments to the proposed Code in response to some of the points raised, the Authority is of the view that the Code Amendment is for the long-term benefit of consumers.

3.5. The Code greatly reduces the likelihood of inefficient price discrimination occurring, which avoids the potential for additional electricity costs to consumers in the order of hundreds-of-millions of dollars per annum. It also mitigates the existence of subsidies which can lead to efficiency losses in the order of tens-of-millions per annum.[1]

3.6. Moreover, the Code imposes relatively low compliance costs on major generators. It is reasonable to expect the information required to be disclosed to the Authority in support of enabling a MLC would be produced by the generators, when they themselves are negotiating and evaluating the commercial merits of the arrangement. The Authority considers these costs are proportionate and will not be a material obstacle to legitimate commercial contracts being entered. Furthermore, the voluntary clearance regime enables parties to MLCs to gain assurance that the arrangement is permissible and won't be subject to future challenge. Finally, the Authority has addressed concerns that the amendment might unintentionally act as a barrier to investment in new clean generation at scale.

4. The Authority has received and considered feedback on the proposed Code amendment

4.1. The Authority consulted on a proposed Code amendment in August 2022. The consultation paper and submissions are available on the Authority's website. The Authority has considered the feedback received and has set out its responses below.

4.2. The Authority received 17 submissions on Inefficient Price Discrimination in very large electricity contracts from the submitters listed in Table 1 below.

Table 1: List of submitters

Category	Submitter
Generators/generator-retailers	Contact Energy Genesis Manawa Mercury Meridian Energy
Retailers	The Independents - 2degrees, Electric Kiwi, Flick, Haast Energy and Pulse Energy Electric Kiwi and Haast

[1] Inefficient Price Discrimination in the Wholesale Electricity Market – Issues and Options, Electricity Authority, October 2021.

Large users	Fonterra Major Energy Users Group (MEUG)
Other	Consumer Advocacy Council (CAC) Business NZ Energy Council Elemental Group Energy Trusts of New Zealand (ETNZ) Entrust Firstgas Fortescue Future Industries (FFI) Vector

Decision to implement the Code amendment despite mixed feedback

4.3. The feedback received from submitters on the proposed Code amendment was mixed, with submitters opinions largely aligning by category type. The Authority also received a broader range of submissions in response to the consultation paper compared to the Issues Paper. This includes submissions from consumer representatives and parties potentially involved in contracts captured by the proposed Code amendment. Feedback from submitters generally fell into two categories: feedback on the problem definition and the proposed Code amendment.

Feedback on the problem definition

4.4. The major generator retailers, most large users and a few other submitters disagreed with the problem definition and therefore did not consider a Code amendment was necessary or would improve outcomes for consumers.

4.5. Arguments made included that the Tiwai contracts reflected a unique situation and are unlikely to be repeated in the future. For example, it was suggested there is a lower risk of inefficient contracts in future due to new investment to improve supply and address transmission constraints, as well as efforts to attract new load to create greater competition. Even if there are two or three contracts a decade, inefficient price discrimination is not a systemic issue which warrants intervention.

4.6. Another argument was that generators have limited incentives to enter inefficient contracts – that generators don't have incentives to price below cost, as too much risk is involved in predicting the market response. Entering inefficient contracts could also have a significant reputational risk which could affect generator-retailers' social license.

4.7. It was also argued that there is a lack of evidence to support intervention. Some submitters argued the Authority did not determine the Tiwai arrangements were inefficient and there is not a robust theory to show that inefficient price discrimination is likely to occur in future.

4.8. The independent retailers and lines companies/representatives that provided submissions, along with CAC and FFI, were in general agreement with the problem definition. This group was broadly supportive of the Authority's analysis and argued that the risk of inefficient price discrimination is real and can lead to adverse outcomes for consumers, including small consumers. Many in this group argued that market power is the root cause of inefficient price discrimination, and that the Authority should address market power more directly.

4.9. The Authority remains of the view that there exists a potential for inefficient price discrimination in the future, notwithstanding the uniqueness of the situation pertaining to Tiwai; the potential efficiency losses and costs to consumers are non-trivial; and the costs of compliance are relatively small when compared with these harms and the risk to public confidence in the market.

4.10. The Authority is concerned that, in the absence of an expectation of a timely and competitive response, generators have incentives to enter, modify, or extend inefficient arrangements with respect to contracts:

(a) which involve a 'credible threat to consumption' – that is, they relate to a customer likely to otherwise exit or not enter the market (ie, not be attracted to locate domestically) or a customer who otherwise would reduce or not expand consumption,

(b) where the contract price is conditional on the consumption of a quantum of electricity by the designated large load user; and

(c) where the quantum of electricity involved is sufficiently large to materially increase prices being faced by other consumers (ie, that are not party to the arrangement).

4.11. Although there may be a very low number of contracts with the potential to satisfy these conditions, they are significant in terms of the share of national generation they are allocated and the potential for severe adverse impacts on consumer outcomes where they are inefficient. There are indications that a number of negotiations over consumption arrangements which meet these conditions will occur in the near to medium term. Examples include a possible new, modified or extended electricity contract for NZAS in advance of the conclusion of the current contract in 2024, and negotiations arising through the market development efforts of generators, most notably Meridian and Contact, to attract large load users such as a hydrogen plant and data centres to the lower South Island.

4.12. It is imperative that the appropriate solution to align generators' incentives with wider society's interests are in place as soon as possible to ensure market participants are confident that any future arrangements are efficient and in the long-term interests of all consumers. Contracts of this scale and upon which investment is contingent would likely be negotiated well in advance of the termination of any existing contract or breaking of ground on new investments. It is possible that any new contracts could have terms extending into decades. The adverse efficiency and wealth consequences of these contracts could be experienced for many years depending on the speed of the competitive response to provide sufficient net new investment in generation to replace the capacity committed the large load user. The Authority is of the opinion that the efficiency costs and wealth transfers associated with these arrangements are of a scale, even in the short term alone, to warrant interventions when they can be shown to be cost effective.

4.13. The Authority sets out its fulsome view of the problem definition in Section 4 of the *Consultation Paper*.

4.14. The Authority notes that the wider wholesale market competition issues that submissions raise were considered in the *Market Monitoring Review of Structure Conduct and Performance in the Wholesale Market*, published in October 2021, and the subsequent *Promoting competition in the wholesale electricity market in the transition toward 100% renewable electricity – Issues Paper*. The Issues Paper proposed that the best approach to promoting competition in the wholesale electricity market in the transition towards a renewables-based electricity system involved proactive monitoring of trading conduct, promoting more and faster entry of supply, and promoting greater demand flexibility and demand participation. This included proposed actions to gather information on contracts to understand and build the evidence base about the nature and scale of current and emerging access issues, and the investigation of the application of trading conduct rules to forward markets.

4.15. The Authority is currently considering submissions on the Issues Paper and its response to submissions on that paper will consider the wider issues on wholesale electricity market competition that submitters have raised, including perceived issues with vertical integration, generator-retailers' internal transfer pricing and unequal access to hedging arrangements.

Feedback on the proposed Code amendment

4.16. Despite some submitters' objection to the problem definition, many indicated that the Code was workable with some modifications. Generator-retailers, large users and some other submitters suggested changes which would reduce uncertainty and improve the clarity of the Code. Independent retailers, consumer representatives and some other submitters similarly made suggestions to improve the intent of the Code amendment. In addition, they made suggestions which they consider would provide stronger protections for consumers. The Authority is appreciative of these submitters offering constructive solutions to improve the effectiveness and efficiency of the Code amendment and minimise the potential for unintended consequences. Modifications suggested by submitters are discussed below and a number of the proposals offered have been adopted in the final Code amendment.

Evaluation criteria and cost benefit analysis

4.17. The Authority also invited feedback on other aspects of the Consultation Paper, including the criteria to evaluate policy options against and the evaluation of the proposed Code amendment against the status quo. Submitters did not provide any comment on these topics, so they are not discussed in the responses to submissions below.

4.18. The changes to the final Code amendment in response to submissions, and discussed below, do not materially change the Authority's evaluation and cost benefit analysis as set out the Consultation Paper. As such, the Authority considers the final Code amendment promotes competition and efficiency and is in the long-term interests of consumers.

Transitional arrangements

4.19. The Code also revokes the urgent Code and provides transitional arrangements should any clearance applications be received prior to revocation, see clause 13.282. The transitional arrangements are a necessary requirement of moving from urgent Code to permanent Code.

Reponses to issues raised in submissions

4.20. The Authority has determined to address inefficient price discrimination directly through a Code Amendment. The remainder of this paper focuses on the issues raised about the draft proposed Code amendment itself and how it might be improved. The suggestions and concerns by submitters are grouped in the following categories:

(a) Definition of a materially large contract

  (i) Definition of Materially Large Contract: "relates to the physical consumption of electricity"

  (ii) 150 MW size threshold

  (iii) Unclear what counts as "built as a consequence of the contract" and "new generation"

  (iv) Interrelated contracts

  (v) Assurance a proposed contract is not a Materially Large Contract

  (vi) Mandate contract price should be subsidy free

  (vii) Other submissions on the definition of a Materially Large Contract

(b) Restriction on materially large contracts

(i) Positive net value test

(ii) Clarification of on-selling terms

(iii) The MLC test in clause 13.269(1) and (2) should be an "and" not "or" condition

(c) Disclosure of materially large contracts

(i) Compulsory disclosure requirements are too onerous and can be simplified

(ii) Simplifying disclosure requirements for contracts which allow on-selling

(d) Clearance regime

(i) Clearance regime timeframes and other matters

(ii) Changes to a cleared contract

(iii) Requirement to publish the outcome of a clearance application

(iv) Rulings Panel should be able to direct the Authority

4.21. The Authority has evaluated the feedback and in places has made changes to the proposed Code amendment as consulted on. The changes do not alter the policy intent of the Code amendment, but the Authority has determined the policy intent is better achieved with these changes. Appendix A sets out the Code amendment with the changes tracked in the text.

4.22. All written submissions have been reviewed and considered by the Authority in reaching the decisions set out in this paper. The Authority has endeavoured to accurately summarise the main views expressed below. However, adopting a generally thematic discussion of the submissions received necessarily compresses the information provided in submissions and the summaries below are not exhaustive. The individual submissions should be read to obtain a full account of submitters' views.

5. Definition of a materially large contract

Definition of a materially large contract that "relates to the physical consumption of electricity"

What the Authority proposed

5.1. Several submitters commented on the definition of a Materially Large Contract and this section discusses submissions on clause 13.268(1)(a)(ii).

5.2. The originally proposed clause 13.268(1)(a) provided that a Materially Large Contract is a contract that:

(a) is not entered into through a derivatives exchange; and

(b) relates to the physical consumption of electricity; and

(c) relates to a net quantity of electricity that equals or exceeds 150 MW consumed at a point in time.

5.3. Clause 13.268(1)(b) provided that two or more contracts will be treated as a MLC if they each satisfy clause 13.268(1)(a)(i)-(ii) and when taken together satisfy paragraph clause 13.268(1)(a)(iii) and meet one of the descriptions in (b)(i) to (iv).

Issue raised by submitters

5.4. Meridian, Contact and Manawa argue the definition of a MLC could be made clearer.

5.5. Meridian suggests more clarity is required around when a contract "relates to" physical consumption.[2] They note, as examples:

(a) that derivatives are based on notional quantities and will not relate to physical consumption. However, all derivative contracts that settle dependent upon prices in physical markets (e.g. the spot market) are in some way therefore related to physical consumption

(b) All contracts where the buyer is acting in the interests of physical consumers could be interpreted as being captured by the clause. Alternatively, Meridian considers the clause be interpreted as limited to the buyer having direct control, or only applies to contracts that include terms that "relate directly to physical consumption, for example, a contractual requirement to consume a certain volume".

5.6. As a consequence, Meridian proposes a more fulsome definition, perhaps including examples.

5.7. Manawa is concerned "physical consumption of electricity" could result in contracts for differences (CFD), which the Tiwai contracts are, being considered a financial contract and not a physical contract. They also highlight that a broader interpretation could be interpreted "to apply to physical supply of electricity by a generator to a retailer for any purpose". Manawa asks that the proposed drafting be reviewed "to ensure the purpose is achieved without creating any unintended consequences".[3]

5.8. Contact notes that the consultation paper highlights the Authority's concern is limited to "where the contract price is conditional on the consumption of a quantum of electricity by the designated load user". They recommend deleting the current clause 13.268(1)(a)(ii) and replacing it with "in which the effective price per MWh payable by the buyer to the seller is increased if the buyer's physical consumption decreases."[4]

5.9. Mercury consider the Code should only apply to MLCs between generators and large load users.[5]

5.10. The Consumer Advocacy Council (CAC) suggest the clause be reworded to account for financial contracts that deliver the same effects as a physical contract[6].

Authority's response

5.11. The Authority's aim is for the Code amendment to have a definition of MLCs which only targets, as best it can, those arrangements which raise the potential for inefficient price discrimination. Such an approach minimises compliance and administration costs, as well as reduces the risk of any unintended consequences and commercial uncertainty.

5.12. Having considered the issues raised by submitters, the Authority considers the originally proposed clause 13.268(1)(a)(ii) should be amended. However, the amendment proposed by Contact is too restrictive because, while price might typically be expected to increase the less that is consumed, this may not always be the case.

5.13. The risks of inefficient price discrimination only exist where there is a credible threat to consumption, say from a prospective buyer exiting or not expanding. Absent this credible threat, any subsidisation of the buyer by the seller is primarily a wealth transfer between the two parties – the subsidised price might impact the buyer's consumption at the margin, but this will have a lesser effect than where the buyer could (and likely would) have exited or not entered the market absent the subsidy. The efficiency considerations are more "second-order" effects when compared with the situation where the buyer could credibly

[2] See page 8 of Meridian's submission.
[3] See page 2 of Manawa's submission.
[4] See pages 10-11 of Contact Energy's submission.
[5] See page 3 of Mercury's submission.
[6] See page 4 of Consumer Advocacy Council's submission.

exit, and the potential increase in prices facing other consumers, because the buyer consumes significantly more load due to the subsidy, is much reduced.

5.14. As a consequence, the Authority considers contracts with buyers, or the load users they are acting for, that do not have a credible threat to consumption should be excluded. In particular, retailers may enter large contracts, however, there is no associated credible threat to the underlying consumption – the retailer acts for a large number of small residential and commercial customers. It is most unlikely this group of consumers could provide a credible threat to national demand, as these parties are in large part committed to residing and operating in New Zealand.

5.15. The Authority has therefore determined to amend clause 13.268(1)(a)(ii) to: *"Includes terms under which the buyer itself will consume electricity."*

5.16. Moreover, the Authority will consider publishing a guidance note, explaining the working of the amendment and this will include the types of contracts which are and are not covered by the definition.

150 MW size threshold

What the Authority proposed

5.17. The originally proposed clause 13.268(a)(iii) provided the size threshold for a materially large contract, a contract that:

(a) relates to a net quantity of electricity that equals or exceeds 150 MW consumed at a point in time.

Issue raised by submitters

5.18. The CAC suggests it should be made explicit that the 150 MW applies to a single 30-minute period over the contract term. They also suggest an annual quantity threshold is added to capture contracts close to but below 150MW, as they consider "the demand and volume could individually have a material effect on wholesale price"[7].

5.19. Independent retailers propose the threshold be defined as 150MW and/or 1,314,000 MW/h over any 12-month period[8].

5.20. Rather than a fixed 150 MW, Fortescue Future Industries (FFI) suggests a flexible threshold e.g. 2% of total system demand[9].

5.21. FFI considered that net 150 MW is likely the right magnitude at this time and Vector thought the threshold was reasonable[10].

Authority's response

5.22. The Authority does not consider changes to clause 13.268(a)(iii) are required.

5.23. Clause 13.268(1)(a)(iii) states the threshold as being "150 MW consumed at a point in time". Moreover, clause 13.268(3) provides that where a contract provides for varying quantities of electricity consumption, the maximum is used for determining whether the threshold is met. The contract only needs to provide for a single instance of 150MW generation over the term of the contract to qualify. 1,314,000 MW/h is the equivalent of 150MW of generation continuously for 365 days, so is already contemplated by the 150MW threshold.

5.24. The provisions in clause 13.268(1)(b) are intended to capture, among other things, situations where a series of contracts, each under 150MW, add up to 150MW. The

[7] See page 4 of the Consumer Advocacy Council's submission.
[8] See page 5 of the independent's submission.
[9] See page 5 of Fortescue Future Industries' submission.
[10] See page 4 of Vector's submission.

Authority considers 150MW is an appropriate threshold for contracts in the New Zealand market of sufficient scale to materially impact general wholesale prices.

5.25. A threshold that varies as a percentage of system demand has the possible advantage of evolving as demand changes over time. However, a fixed MW threshold has the advantage of greater certainty and avoids doubt whether the Code applies to a contract or not. On balance, the Authority has decided to retain a net 150 MW threshold.

Unclear what counts as "built as a consequence of the contract" and "new generation"

What the Authority proposed

5.26. As part of the definition of a MLC, the originally proposed clause 13.268(4) stated "the net quantity of electricity is the total MW consumed at a point in time (calculated in accordance with subclause (3)) less any MW consumed from new generation built as a consequence of the contract". For the purposes of the 150 MW threshold, the net quantity of electricity is the total MW consumed at a point in time (calculated in accordance with clause 13.268(3)) less any new generation built as a consequence of the contract.

5.27. In clause 13.268(3), where an MLC allows for varying quantities of electricity consumption at one point in time, the maximum quantity of electricity consumption possible under the contract at any one time is to be used for the purpose of determining whether the MW threshold is met.

Issue raised by submitters

5.28. Firstgas Group, Contact and Genesis consider the proposed drafting of clause 13.268(4) is unclear and will create uncertainty and costs higher than anticipated by the Authority.

5.29. FirstGas recommends replacing "built as a consequence of the contract" in clause 13.268(4) with "substantially underwritten by the contract". It suggests that, other than in clear cut cases, the phrase "built as a consequence", will cause risk-averse parties to assume that their contract might be captured by the definition. FirstGas suggests that a party signing off an investment in new generation, without first getting signed contracts with cornerstone customers, would face uncertainty as to whether the regulator would consider the investment was a consequence of the prospective future contracts.

5.30. Firstgas recommends replacing "new generation" in clause 13.268(4) with "additional generation capacity". They provide a number of examples where "new" generation might be ambiguous or undermine the policy intent. Examples, include whether the following should be considered "new generation":

(a) a generator replacing end-of-life generation with like-for-like

(b) fossil-fuelled thermal is replaced or converted to bio-fuelled thermal generation

(c) the turbine blades of an existing wind farm are replaced

(d) a new thermal plant is commissioned but to utilises heat from a geothermal resource used by an existing generator.[11]

5.31. Genesis argues the current drafting may impede contracts supporting new generation. They propose replacing "as a consequence of" with "in connection with", reflecting there is more than one driver of new generation and to mitigate the risk that the current drafting might unintentionally exclude new generation supported by a MLC. They also suggest that a definition of "new generation" is required covering situations where the generation is

[11] See pages 2-3 of Firstgas Group's submission.

proposed to be built in stages with PPAs or options underwriting these, and exiting plant is being refurbished or repowered[12].

5.32. Contact raises the concern that the wording "as a consequence" raises uncertainties, including:

(a) whether the clause captures contracts linked to load, such as variable volume CFDs, as well as fixed volume CFDs

(b) what impact timing of the contract has, including whether it needs to be place prior to the decision to invest in new generation

(c) whether the contract can relate to existing demand

(d) any particular conditions on the contract that may preclude it from being essential to renewable generation build

5.33. Contact points out that Concept Consulting has noted that "developers are signalling willingness to take a degree of offtake risk – a notable difference to the past", for reasons including "greater comfort based on market soundings that consumers will be willing to enter into contracts once a project is completed." Contact suggests that "the timing of an offtake agreement should not diminish its importance in supporting new generation. Even though a contract may be entered into well after a final investment decision, the investment was only undertaken because of an expectation of being able to reach an offtake agreement at a later date. Under the current drafting there is no certainty how timing of contracts will be treated."

5.34. Contact proposes the following redrafting of clause 13.268(4):

> *For the purpose of subclause 1(a)(iii), the net quantity of electricity is the total MW consumed at a point in time (calculated in accordance with subclause (3)) less an MW contracted in respect of new generation where the contract, or the anticipation of a fixed price power purchase agreement or CFD with the buyer or a third party, must be a material factor for the generator in constructing the new generation. In determining whether this clause13.268(4) applies:*
>
> *(i) the contract can relate to a buyer's new or existing demand for electricity; and*
>
> *(ii) the timing of the execution of the contract will not be relevant.*[13]

5.35. Firstgas consider clause 13.268(4) results in better outcomes for existing owners of generation plants. They have interpreted the clause to mean that if an existing generator supplies new and existing generation in a single supply contract, the 'exclusion' under clause 13.268(4) applies to all generation supplied in a single contract, including both intermittent and firming generation, whereas they consider this isn't the case where a new generator provides intermittent generation, and the firming is provided by an existing generator.

5.36. Firstgas provide two hypothetical examples to demonstrate this point:

(a) Example 1: a new 500 MW windfarm and a generator providing 300 MW of existing generation have separate supply contracts with a 300 MW load user.

(b) Example 2: an existing generator with a new 500 MW windfarm and 300 MW of existing generation supplies a 300 MW load user under a single contract.[14]

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[12] See page 2 of Genesis's Schedule 1: Feedback on Proposed Part 13 Subpart 7 Code Provisions.

[13] See pages 12-14 of Contact's submission.

[14] See pages 2 and 3 of Firstgas Group's submission.

Authority's response

5.37. The Authority is committed to achieving its policy intent while mitigating avoidable sources of uncertainty arising from the Code amendment, which could dampen investment in new and efficient (renewable) generation.

5.38. The Authority agrees that there is often more than one driver underlying an investment decision, and therefore the phrase "as a consequence of" could be perceived as too restrictive and definitive to demonstrate. The phrase "in connection with" is also not appropriate, as the contract should be a major catalyst for the new investment not just a factor. The Authority has determined to replace the current wording with the concept of the contract being "material" in the generator's decision to invest in new generation.

5.39. The Authority's policy intent by allowing an offset for any "new generation", when determining the threshold for a MLC, is to acknowledge any investment resulting in marginal generating capacity at a point in time which is conditional on the contract. The relevant considerations are whether the investment provides marginal generating capacity at a point in time and is unlikely to happen absent the contract. As such, the form of the investment is less important, including refurbishing and repowering investments. Therefore, so long as it can be shown that the contract is a material factor in the investment decision making many of the examples provided above by the submitters should be allowable offsets, such as:

(a) Completely new generation

(b) A like-for-like replacement of end-of-life assets

(c) Fossil-fuelled thermal conversion to bio-fuel.

(d) Replacement of turbine blades on an existing windfarm

(e) A new thermal plant which increases whole of system MW capacity at a point in time.

5.40. Both fixed and variable volume CFDs are potentially covered, so long as they meet the other attributes of a MLC (see clause 13.268 - Definition of materially large contract). So it would exclude contracts that are entered through a derivatives exchange, do not include terms under which the buyer itself will consume electricity and are less than net 150 MW.

5.41. The contract can relate to both a buyer's existing and new demand. For example, a generator could enter a 200 MW PPA contract with a pre-existing load user and rely upon that contract to underwrite 75MW of new generation. The contract would not meet the net 150 MW threshold for a MLC if it can be shown the 200 MW contract was material in the generator's decision to invest in the 75MW of new generation. This would involve the generator demonstrating that the investment would not have otherwise happened – this would presumably be easier to demonstrate if the buyer's demand would have exited or been much less if the contract did not happen. The Authority also notes that, as with the clearance process, generators are free to have informal discussions with Authority staff about deal structures and the potential application, or not, of the Code amendment. The Authority encourages such discussions at an early point albeit that no assurances would be given outside of the formal processes.

5.42. The Code provides for netting purposes, any promised future new generation can be offset against a load at a point in time. However, if net load at any point in time during the term of the contract is expected to exceed 150MW, then the contract would be deemed a MLC. Clause 13.268 (1)(a)(iii) concerns net consumption exceeding 150MW "at a point in time". Therefore, a contract for a flat 200 MW for the entire period of the contract, but underwritten by a new 200MW dispatchable generating asset which will be commissioned 12-months after the 200MW supply contract commences, would be judged a MLC (net electricity consumed over the first 12 months exceeds 150 MW). Moreover, if this contract for 200 MW of demand was underwriting a windfarm with 1,000 MW max generation, it would be considered a MLC if the buyer's right to consume electricity under the contract exceeds 150 MW above the actual generation from the windfarm at any point in time eg. if

the contract is for a fixed 200 MW, even when the new windfarm is producing less than 50 MW.

5.43. At the time of signing a contract, expected investment in new generation may mean the contract is not an MLC (on account of the netting of the volume of new generation e.g. a contract for 100MW in the first year, stepping up to 200MW in the second year, coupled with the commissioning of a 150MW of new generation from month 12 onwards[15]). However, if the new generation is not built, delayed or downsized, such that the net load under the contract exceeds the net 150MW threshold for any period, then, at that time, the contract would constitute a MLC and the restriction of MLCs would be engaged from that point onwards.

5.44. To address this issue, the Authority has decided to make two changes to the Code. The first is to extend the disclosure obligations by including an additional clause 13.271(1)(d):

> a change to the volume or timing of any new generation taken into account in reliance on clause 13.268(4) where:
>
> (i) the quantity of electricity generated from new generation has decreased; and
>
> (ii) the net quantity of electricity for any contract exceeds the threshold in clause 13.268(1)(a)(iii).

5.45. Secondly, to extend the circumstances in clause 13.273(6) where a clearance provided by the Authority does not apply to include:

> a change to the volume or timing of any new generation taken into account in reliance on clause 13.268(4) where:
>
> (i) the quantity of electricity generated from new generation has decreased; and
>
> (ii) the net quantity of electricity for any contract exceeds the threshold in clause 13.268(1)(a)(iii).

5.46. The Authority does not support the general suggestion that an investment in generation which is already approved, under construction or completed, should be permissible as an offset against future contracts. The investment is at that time a sunk cost and should be treated consistently with other established generating assets, facing the decision whether to continue operating and on what terms. It is difficult to conceive of a contract being material to the investment decision, when the contract is not finalised before the new investment is committed to.

5.47. Allowing new but already approved generation investments to be claimable as an offset against future large load contracts would create a significant potential for gaming to avoid the intent of the Code. Moreover, the Authority does not consider precluding these "new but approved" investments in generation as an offset will have a material impact on investment in renewable generation. Investors which have committed to investing in new generation prior to signing offtake contracts can mitigate any risk of falling foul of the Code amendment by allowing a buyer to on-sell the electricity (or show that the value of the contract to them exceeds the alternative). The Authority understands it would be unusual for a generator, seeking to underwrite new investment, to restrict the buyer's ability to on-sell the electricity. The investor's primary concern should be with contracting for offtake at a price sufficient to secure financing and earn an appropriate return (and not who is consuming that electricity).

5.48. The Authority considers the second use of the word "consumed" was potentially confusing in this clause and considers that clause 13.268(4) should be amended to read:

> *…the net quantity of electricity is the total MW consumed at a point in time (calculated in accordance with subclause (3)) less any MW generated from new generation,*

[15] In year one the net load is 100 MW, and 50 MW (200-150) in year 2. At no point in time is the net MW > 150MW.

where the materially large contract is material to the generator's decision to invest in the new generation.

5.49. The Authority does not agree with Firstgas's interpretation that clause 13.268(4) provides better outcomes for existing generators. Clause 13.268(1)(a)(iii) relates to a net quantity of electricity that equals or exceeds 150 MW consumed at a point in time. In both examples provided by Firstgas, the sum of contracts would meet the 150 MW threshold where it is reasonable to expect that there will be points in time during the term of the contract - when there is not enough wind – requiring the existing firming generation to supply at least 150 MW to the load user. To be clear, the 500 MW windfarm in both examples is not exempt from complying with the Code. All individual contracts supplying the load user and satisfy the MLC definition are captured under clause 13.268(1)(b).

Interrelated contracts

What the Authority proposed

5.50. The proposed Code amendment included provisions to ensure the intent of the Code changes are not undermined by generators changing contract structures to avoid the net 150 MW threshold. Clause 13.268(1)(b)(i) to (iv) target likely structures that could be used to avoid the intent of the Code.

5.51. In the originally proposed Code amendment, a MLC is two or more contracts that each satisfy clause 13.268(1)(a)(i)-(ii) and, when taken together, equal or exceed net 150 MW (clause 13.268(1)(a)(iii) and meet one of the following descriptions:

(i) two or more contracts between a generator and a buyer; or

(ii) at least one contract between a generator and a buyer and at least one contract between that generator and its related company and that buyer or its related company; or

(iii) at least one contract between a generator and a buyer and at least one contract involving a second generator where the contracts rely on each other or are otherwise interdependent; or

(iv) any other arrangement that is substantially of the same kind as that described in any of subparagraphs (i)-(iii)

5.52. Clause 13.268(1)(b)(iv) provided a 'catch-all' clause to capture any other arrangement which avoids the intent of the Code but is not explicitly described in (i) to (iii). The purpose of this clause is to protect consumers as the Authority may not foresee all types of contract structures.

5.53. The proposed Code amendment required each individual generator involved in a related contract scenario to comply with the prohibition and disclosure requirements provided in clause 13.268(2):

For materially large contracts made up of two or more different generators' contracts, any reference to materially large contract in the following clauses must be read as only referring to an individual generator's contract(s) that forms part of a materially large contract, rather than as a reference to the multiple generators' contracts.

Issue raised by submitters

5.54. Most submitters agreed with the intent of the Code. However, some submitters think the Authority could provide more clarity in the drafting of clause 13.268(1)(b)(iii) and (iv).

5.55. Contact suggested the Authority should amend clause 13.268(1)(b)(iii) and clarify when two contracts are considered to rely on each other. It is unclear whether this clause means contracts that explicitly reference another contract e.g. where a contract only comes into force if other load is also procured. Or, irrespective of the drafting of the contract, two contracts could rely on each other if there are two or more generators providing load to a

single user which sums to more than 150 MW. In practice generators would need to know the load and nature of a second contract and this could put generators in breach of competition law. Contact recommends amending this provision to:

> *"at least one contract between a generator and a buyer and at least one contract involving a second generator where the contracts contain interdependent terms in relation to any matter relating to price, volume or effectiveness."*[16]

5.56. Genesis raised concerns with clause 13.268 (1)(b)(iii) that there may be cases where a PPA is up for renewal and a generator sells to more than one buyer, with different volumes and at different points in time for commercial reasons. A generator should be free to sell to more than one buyer at different points in time. Genesis suggests amending this provision to:

> *"at least on contract between a generator ("first generator") and a buyer and at least one contract involving the first generator and a second generator where the contracts are entered into contemporaneously with each other, and which rely directly on each other or are otherwise interdependent."*[17]

5.57. Meridian suggests the Authority should further explain or delete clause 13.268(1)(b)(iv) as it is unclear to generators what the Authority might mean.[18]

5.58. Firstgas states the Authority anticipates that a mix of contracts with existing and new generation will be needed to supply new loads in the transition with clause 13.268(2). However, clause 13.268(2) will not give effect to the intention with enough clarity. Firstgas suggests changing clause 13.268(2) to:

> *"If two or more contracts are considered related for the purpose of subclause 13.268(1) but do not collectively meet the conditions in subclauses (1)(a)(i) – (iii), each related contract cannot be a materially large contract."*[19]

Authority's response

5.59. The Authority has elected to restructure clause 13.268, by transferring content from the originally proposed clause 13.268(1)(b)(i)-(iv) to a new clause 13.268(1)(c) and to expand clause 13.268(1)(b).

5.60. The Authority's intention was that the originally drafted clause 13.268(1)(b)(iii) would capture contracts that either implicitly or explicitly rely on each other. Therefore, the Authority rejects Contact's suggestion that the clause (now contained in clause 13.268(1)(c)(iii) and (iv)) should only capture contracts that explicitly rely on each other. The Authority considers that Contact's suggestion is likely to be too narrow, and it is in the long-term interests of consumers for the Authority to have visibility of contracts with the potential to enable inefficient price discrimination.

5.61. Contact observes that generators may not know whether contracts implicitly rely on each other as they do not have visibility of other generators supplying a large load user. However, the Authority considers a generator will often be able to imply this given public knowledge about minimum viable load requirements of major load users. If a generator only supplies a portion of a large load user's minimum viable consumption it can assume there may be other related contracts, unless it has reason to believe that the load user is relying upon spot contracting for the rest of its load. Generators can also approach the Authority on an informal basis to discuss contracts. Moreover, if a generator wanted assurance about a proposed arrangement they could seek a clearance, even when they do not think one is required.

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[16] See pages 11-12 of Contact's submission.
[17] See page 1 of Schedule 1 of Genesis's submission.
[18] See pages 10-12 of Meridian's submission.
[19] See page 3 of Firstgas Group's submission.

5.62. The Authority recognises this situation may result in generators disclosing some contracts that ultimately prove not to be MLCs. However, the Authority considers the additional compliance costs this imposes is small relative to the potential harm where inefficient price discrimination occurs.

5.63. In response to the issues raised by Genesis and Contact, the Authority has decided to replace the originally proposed clause 13.268(1)(b)(iii) with two separate clauses 13.268(1)(c)(iii) and (iv)[20] to provide more clarity.

> *13.268(1)(c)(iii) at least one contract between a generator and a buyer and at least one contract involving a second generator and the same buyer where the contracts rely on each other or are otherwise interdependent ; or*
>
> *13.268(1)(c)(iv) at least one contract between a generator and a buyer and a contract between the same generator and a second generator where the contracts rely on each other or are otherwise interdependent.*

5.64. These clauses will provide greater clarity to generators and ensure the drafting of the Code amendment is targeted only at situations where there is the potential for inefficient price discrimination. This will reduce the risk of generators disclosing or going through the clearance process where contract structures do not have the potential to create the conditions for inefficient price discrimination the Authority is seeking to address.

5.65. However, the Authority rejects Genesis's suggestion to amend the originally proposed clause 13.268(1)(b)(iii) to refer to "contracts entered into contemporaneously with each other, and which rely directly on each other or are otherwise interdependent."[21] It is possible that interrelated contracts may be entered at different points in time (i.e. not contemporaneously) but may create the conditions for inefficient price discrimination.

5.66. The Authority has also decided to amend clause 13.268(1)(b) following the change to clause 13.268(1)(a)(ii) above. This change means that individual contracts which may not meet the requirements of clause 13.268(1)(a)(ii) but are relied on by or are interdependent with another generator's contract which does meet the requirements of clause 13.268(1)(a)(ii), are captured by the Code if when taken together with the other contract(s) they meet the 150MW threshold (clause 13.268(1)(b)(iii)). The Authority considers it is important to capture these contracts due to the potential for them to form part of a wider subsidy and inefficient price discrimination arrangement. The Authority has decided to amend clause 13.268(1)(b) to:

> *…two or more contracts where:*
>
> *(i) all the contracts satisfy paragraph (a)(i);*
>
> *(ii) at least one contract satisfies paragraph (a)(ii); and*
>
> *(iii) the contracts when taken together satisfy paragraph (a)(iii) and meet one of the descriptions set out in paragraph (c) below:*

5.67. The Authority has decided to retain a catch-all clause as it is not possible to foresee all types of contract structures in the future. Changes to (now) clauses 13.268(1)(c)(iii) and (iv) should provide generators greater clarity over the types of contract structures the Authority intends to capture. The catch-all clause now contained in clause 13.268(1)(c)(v) remains substantively the same and reads:

> *any other arrangement that is substantially of the same kind as that described in any of subparagraphs (i)-(iv).*

5.68. The Authority will monitor clause 13.268(1)(a) – (c) and could refine clause 13.268(1)(c) in the event of generators disclosing contract(s) which the Authority considers not to be

[20] With the existing clause 13.268(1)(b)(iv) becoming clause 13.268(1)(c)(v).
[21] See page 1 of Schedule 1

materially large contracts. A future change may be warranted if the current clauses are imposing unreasonable compliance costs on generators, and the public policy interest can be achieved more efficiently.

5.69. The Authority has determined not to make changes in response to Firstgas's suggestion to amend clause 13.268(2). The Authority considers related contracts are only every considered a MLC where the contracts together satisfy the MLC definition in clause 13.268(1)(a).

5.70. As discussed above, there may be cases where a generator only has partial visibility whether its contract is part of a MLC. Where a generator can reasonably expect that an individual contract may be related to other contracts that form a MLC, the generator can seek assurance whether its contract is in breach of the Code amendment or not by complying with the requirements under Part 13, subpart 7. The Authority considers it is proportionate to have visibility of individual contracts with the potential for inefficient price discrimination given the compliance costs to generators are minimal relative to the size of the potential harm to consumers.

Assurance a proposed contract isn't a materially large contract

What the Authority proposed

5.71. The proposed Code amendment defined a MLC in clause 13.268 and clause 13.272 set out the application process for a generator seeking clearance.

Issue raised by submitters

5.72. Firstgas suggests adding a new clause 13.272A that enables a generator to seek the Authority's agreement that a set of circumstances mean a prospective contract would not be a materially large contract, provided the applicant's information is complete and accurate.[22]

Authority's response

5.73. Regulators do not usually provide assurance of compliance, but rather investigate and prosecute noncompliance.

5.74. The Authority considers this issue is best managed through a clear and targeted definition for materially large contracts.

5.75. Generators can approach the Authority on an informal basis to discuss contracts. However, if a party wanted assurance about a proposed arrangement they could seek a clearance, even when the generator doesn't think one is required. Moreover, any formal process designed to provide assurance whether a proposed contract is a MLC would be of a similar duration as a clearance and would therefore add little value.

Mandate contract price should be subsidy free

What the Authority proposed

5.76. The originally proposed clause 13.269 outlined the restriction on materially large contracts. A generator must not give effect to a materially large contract unless:

(a) the net value of the materially large contract to the generator calculated in accordance with clause 13.270 is a positive value; or

(b) the materially large contract allows the buyer to on-sell any un-used MW quantities under the materially large contract without the buyer being subject to any worse terms than if it had consumed the relevant quantity itself; or

[22] See page 4 of Firstgas Group's submission.

(c) the Authority has provided a clearance under clause 13.273 in respect of the materially large contract and that clearance remains effective and applicable.

5.77. This clause does not prevent a generator entering into a MLC that is conditional on the Authority clearing the contract, and this clause only applies to MLCs entered into, extended or modified on or after the date this clause came into force.

Issue raised by submitters

5.78. Vector and the Independent Retailers suggest the Code should require that the contract price is subsidy free[23].

Authority's response

5.79. The "net value" to the generator test in clause 13.269(1)(a) is a specific test for a form of subsidy, and applies if a MLC restricts on-selling.

5.80. Where the contract allows the buyer to on-sell consistent with clause 13.269(1)(b), the Authority is comfortable with any contract price (including a subsidy), as providing an on-selling capacity addresses any inefficient price discrimination concerns the Authority might otherwise have with the contract.

Other submissions on MLC definition

What the Authority proposed

5.81. Under the calculation of the net value of a MLC to the generator in the originally proposed clause 13.270, the net value of the MLC to the generator is the value of the contract to the generator less the value of the generator's best alternative. The calculation of these components must take into account any direct value components and assign a monetary value that equates to its value to the generator. Clause 13.270(3) sets out the value components, which may include (without limitation) –

(a) contract price

(b) prices for baseload futures contracts over the period covered by the materially large contract and, where a materially large contract covers a period in time not yet covered by base load futures contracts, the generator's reasonable expectations as to base forward prices over this period:

(c) node location:

(d) load profile differing from base load:

(e) demand response provisions:

(f) price separation provisions:

(g) contract price pegged to an index provision:

(h) value of maintaining an uninterrupted commercial relationship with the buyer:

(i) relative counterparty risk:

(j) any other financial inducements or benefits associated with the materially large contract.

5.82. The list above provides examples and does not limit other direct value components from being taken into consideration. As such, the Authority considers that transmission constraints may be accounted for in the net value test if a generator chooses to rely on the net value test.

[23] See page 4 of Vector's submission and page 5 of the Independent Retailers's submission.

Issue raised by submitters

5.83. Elemental Group were unclear whether offshore wind projects connected directly to consumers with limited grid connectivity would be excluded from the rules.[24]

Authority's response

5.84. The Authority is of the view that contracts with limited grid connectivity, where it is not possible to export net 150 MW or more at a point in time over the life of the contract, do not have the potential to shift market prices for other consumers and enable potential for inefficient price discrimination.

5.85. However, upgrades to grid connectivity over the life of the contract may be foreseen at the time a contract is entered. Even though some MLCs may have limited grid connectivity at the time of signing the contract, a generator may at that time have reason to expect grid upgrades in the future. As such, it is conceivable that contracts may be put in place in advance of a grid upgrade with the purpose to effect inefficient price discrimination.

5.86. Therefore, the Authority wishes to have visibility of all contracts which satisfy the MLC definition and are connected to the national grid. Where a generator expects there is limited grid connectivity over the lifetime of the contract, the "stranded" electricity (i.e. that generation which can't be exported to the grid) in the absence of the MLC will presumably have a very low (even negative) value. However, if the generator can reasonably expect an increase in grid connectivity increasing over the lifetime, the generator ought to account for this in their calculation of the net value of the MLC, if that is the limb they are relying upon for approval.

6. Restriction on materially large contracts

Materially large contract – positive value test

What the Authority proposed

6.1. The originally proposed clause 13.270(2) provided that the calculation of the value of the generator's best alternative must take into account the generator's reasonable expectations as to whether in the absence of the materially large contract the buyer would have exited completely, reduced consumption, not expanded, or not entered the domestic market.

Issue raised by submitters

6.2. Genesis recommends that clause 13.270(2) be deleted. They argue that generators are not privy to buyers' commercial and strategic objectives, and decision processes. Therefore, generators are not well placed to judge a load user's response in the absence of the contract.[25]

6.3. Fonterra is concerned that the definition of "best alternative price" is too vague, and suggest the Electricity Authority consider the role of Long Run Marginal Cost (LRMC) in determining a fair price.[26]

Authority's response

6.4. Clause 13.270(2) is intended to provide the generator with the opportunity to recognise that the absence of the MLC would result in a material difference in aggregate demand, which could explain a significant divergence in the negotiated price and observed national prices with the contract. For example, the Authority considers the credibility of NZAS's threat of exit set the context of negotiations in 2020, and ultimately influenced the agreed contract price. Absent the credibility of that threat, the generators would likely have sought

[24] See Elemental's response to the Authority's question 3 in their submission.
[25] See page 3 of Schedule 1 of Genesis's submission.
[26] See page 2 of Fonterra's submission.

to negotiate a higher price than they did. Clause 13.270(2) requires generators to consider their reasonable expectations of a buyer's response absent the contract, and which would have informed the pricing assumptions they adopted in negotiating a price.

6.5. In the situation posited by Genesis, to satisfy the requirement in clause 13.271(3)((vi) (which requires the generator to provide evidence of its expectations taken into account under clause 13.270(2)) the generator would simply have to state that they have no reasonable expectation of the buyer's response absent the MLC and so none were taken into account.

6.6. In considering the concern raised by Genesis, the Authority has determined not to change the clause.

6.7. With respect to clause 13.270(3)(b), The Authority agrees that modelling of LRMC (and possibly the levelised cost of electricity) may often be used by generators to benchmark pricing in periods extending beyond those covered by base load futures contracts. As such the Authority has added the following words to the end of clause 13.270(3)(b):

> *"…the generator's reasonable expectations as to base forward prices over this period, which may include consideration of the long run marginal cost of electricity, the levelised cost of electricity and other factors."*

Clarification of on-selling terms

What the Authority proposed

6.8. The originally proposed clause 13.269(1)(b) permitted a MLC where the buyer can "…on-sell any un-used MW quantities under the materially large contract…"

Issue raised by submitters

6.9. Genesis proposes that clause 13.269(1)(b) should be updated to so that it specifically states that the buyer isn't "subject to any worse terms under the contract than if it had consumed the relevant quantity itself"[27].

6.10. CAC is concerned the test could be passed by the contract allowing the on-selling of a small quantity of electricity. They propose a requirement that the buyer can on-sell no less than 20% of the unused MW.[28]

6.11. Elemental suggest that consideration for electricity contracts with large exporters of electricity intensive products, such as hydrogen, dairy and aluminium, to contain mandated demand response clauses (say, 15% onselling) that could be called to add capacity during times of scarcity.[29]

Authority's response

6.12. The current drafting provides that the buyer must have discretion to on-sell any of the unused quantity. The intent was that the buyer must have total discretion to on-sell all the unused quantity specified in the contract. To clarify this point the Authority has decided to change clause 13.269(1)(b) to "…on-sell all un-used MW quantities under the materially large contract…"

6.13. Mandating demand response is outside the scope of the inefficient price discrimination problem definition. The Authority continues to have confidence in commercial incentives and the market to develop cost effective and efficient demand response solutions.

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[27] See page 2 of Schedule 1 of Genesis's submission.
[28] See page 4 of Consumer Advocacy Council's submission.
[29] See Elemental's response to question 11 in their submission.

The MLC test in clause 13.269(1) and clause 13.269(2) should be an "and" not "or" condition

What the Authority proposed

6.14. The originally proposed clause 13.269(1) defined the restriction on materially large contracts. A generator must not give effect to a materially large contract unless—

(a) the net value of the materially large contract to the generator calculated in accordance with clause 13.270 is a positive value; or

(b) the materially large contract allows the buyer to on-sell any un-used MW quantities under the materially large contract without the buyer being subject to any worse terms than if it had consumed the relevant quantity itself; or

(c) the Authority has provided a clearance under clause 13.273 in respect of the materially large contract and that clearance remains effective and applicable.

Issue raised by submitters

6.15. The "Independents" comprising (2degrees, Electric Kiwi, Flick Electric, Haast Energy Trading, and Pulse) argue that the requirements in clauses 13.269(1)(a) and (b) of the proposed Code Amendment allowing MLCs should be "and" conditions rather than "or" conditions. That is the generator would be required to show that the direct value to the generator of the contract is positive relative to the generator's best alternative, and that the electricity could be on-sold.

6.16. The Independents are of the view that allowing MLCs which provide for on-selling, without regard for the contract price, does not provide sufficient assurance that electricity is being allocated efficiently. The Independents argue that the buyer may not always on-sell the electricity where it could be sold at a profit relative to using the electricity itself. They point out "other considerations; including that contract negotiation is not a one-off game and what Tiwai does with the electricity it purchases may impact the amount (and price) of electricity Meridian et al are willing to offer in future negotiations." In a repeat game load users may not on-sell because of the threat of receiving less favourable terms when the contract is renegotiated.[30]

Authority's response

6.17. The literature discussed in para 4.28 to 4.36 in the *Consultation Paper* shows that the prevention of on-selling is a necessary condition for a firm to implement a viable price discrimination strategy. Where resale is possible, the segment of consumers with access to lower prices can on-sell to that segment of customers the firm is seeking to charge higher prices to.

6.18. It is for this reason that the Authority has proposed that MLCs are permitted, irrespective of the contract price, where the contract does not restrict the electricity being resold by the buyer. Where the generator sells electricity without restrictions on resale, they are effectively creating a competitor with the capacity to sell electricity at a profit, when the expected future price it can be resold for exceeds the contract price. The lower the contract price the more cost competitive this competitor is. The buyer has the incentive to on-sell where the profit they earn on the resold electricity exceeds what they would earn by using the electricity themselves. Any subsidy provided by the generator is in this case primarily a wealth transfer from the generator to the initial buyer. Absent barriers to on-selling the electricity can be expected to be allocated efficiently to the highest valued user.

6.19. The Authority acknowledges that this is a somewhat static analysis. The Independents point out that in a repeat game a buyer, who enjoys a subsidised price due to a generator's price discriminating practices, may not choose to make a "profit" from on-

[30] See page 5 of the independent's submission.

selling, if there is the possibility that the generator will respond to this practise by offering the buyer less favourable terms in future negotiations. In a repeat game a generator's future negotiating position, including quantity and price, may be conditional on the buyer's consumption versus on-selling decisions in previous periods.

6.20. Where a generator provides a subsidy and allows on-selling, they could theoretically in a limited number of situations avoid the policy intent of the Code. The most obvious means of doing this would be to offer contracts with short terms. Short duration contracts limit the costs to the generator if the buyer elects to on-sell – as the buyer only gets the benefits from on-selling at a profit for the (short) period of the contract. Moreover, because the generator is less likely to offer such subsidised prices in future, the future costs to the buyer, if they intend to resume consumption of electricity, may well outweigh the profits gained from on-selling.

6.21. Implementing this strategy requires the generator to convince the buyer to accept short term contracts. The buyers to materially large contracts will most often be capital intensive business, which face significant stranded asset risk e.g. aluminium and hydrogen plants. Other than in situations where they are reviewing their on-going presence in New Zealand, these buyers would be expected to favour long term contracts, often extending 15 years or more.

6.22. Moreover, changing the condition to an "and" would require all MLCs which pass the "net value" test (clause 13.269(1)(a)) to also allow on-selling. A contract with an efficient price does not raise inefficient price discrimination issues as presented in the problem definition. On-selling restrictions may have legitimate commercial purpose in some cases and prohibiting them for all MLCs could have unintended consequences.

6.23. While acknowledging the point made by the Independents, the Authority considers the condition between clause 13.269(1)(a) and (b) should remain an "or". The buyers to MLC contracts will often face stranded asset risks and will typically have strong commercial incentives to favour long term contracts. Changing the condition to an "and" would effectively mandate that all MLCs must allow on-selling, even though the contract price is efficient, and that alone is sufficient assurance that there no potential for inefficient price discrimination with respect to a MLC. The "or" condition does not unduly restrict flexibility in commercial arrangements, and by providing a relatively straight forward on-selling test (vis-a-via the value test), significantly reduces the compliance and administration costs associated with the Code amendment. The Authority will monitor the duration of future MLCs, and if it appears that short-dated contracts are being used to avoid the intent of the Code, then we will revisit this conclusion.

7. Disclosure of materially large contracts

Compulsory disclosure requirements are too onerous and can be simplified

What the Authority proposed

7.1. The originally proposed clause 13.271(1) stated when a generator must adhere to the disclosure regime. Some submitters commented on clause 13.271(1)(b) and (c) which required a generator to disclose information to the Authority not later than 5 days after making changes to a MLC that may affect the calculation of the net value of a MLC if the generator relies on the "net value" test or changes to a MLC's on-selling arrangements if a generator relies on the "on-selling" test.

7.2. Clause 13.271(2) outlined the information a generator must disclose to the Authority. Submitters commented on clauses 13.271(2)(b), (c) and (d):

- Clause 13.271(2)(b) required a generator to provide a statement of the generator's reasons as to how a MLC satisfies either the "net value" or "on-selling" test.

- Clause 13.271(2)(c) required a generator to provide evidence to support its reasons in its statement.
- Clause 13.271(2)(d) required a generator to disclose any information or documents including any financial modelling, that are in the possession, or under the control, of the generator that discuss or show the impact of the materially large contract on the generator's and its related companies' group-level earnings before interest, taxes, depreciation, amortisation and fair value adjustments or on the generator's and its related companies' broader financial performance and strength.

7.3. Clause 13.271(3) and (4) outlined the evidence a generator must provide under 13.271(2)(c) to show how a MLC satisfies the "on-selling" or "net value test." Submitters commented on the following clauses:

- 13.271(3)(b) and 13.271(4)(b) required generators to disclose all other information and documents that are in the possession, or under the control, of the generator and that are or may be material to an assessment of a generator's compliance with the "on-selling" test or the "net value" test.
- 13.271(3)(a)(v) required a generator relying on the "net value" test to provide a justification for the monetary value assigned to any value component, including any assumptions relied on and (if available) evidence to show whether those assumptions are consistent with similar assumptions being made elsewhere in the generator's business in the 30 business days immediately preceding the date the generator entered into the materially large contract.

Issue raised by submitters

7.4. Several submitters, most notably the major generators, suggested amendments to the disclosure requirements pertaining to MLCs.

7.5. Meridian suggests that the provisions requiring compulsory disclosure of information by the selling party to a MLC should be deleted. They argue that participants should have the option to "self-assess" whether the contract follows the Code. Meridian considers that requiring a participant to disclose information where the seller is satisfied that they are in compliance with the Code is "unnecessary and onerous." They are however open to requiring that participants notify the Authority if they enter a MLC in instances where they have not sought clearance. They say that the Authority could rely upon its powers under section 46 of the Electricity Industry Act 2010 (the Act) to require the provision of information from participants to inform its assessment of the MLC's compliance with the Code.[31]

7.6. Genesis suggests removing "or may be" from clauses 13.271(3)(b) and 13.271(4)(b) as a means of reducing the uncertainty facing generators, and instead rely on generators to determine what "other information" beyond that specified explicitly in clause 13.271(3) is material.[32]

7.7. Submitters including Business Energy NZ and Meridian proposed ways in which the disclosure regime might be streamlined, thereby reducing compliance costs for participants. Submitters proposed that any mandatory disclosure requirements should differentiate between MLC's which the seller believes to be in compliance with the Code because the contract satisfies the "on-selling" test versus contracts satisfying the "net value" test. For example, Meridian suggest where a contract meets the on-selling test (clause 13.269(1)(b)) then it is unnecessary to require the seller to provide information including "financial modelling… show[ing] the impact of the materially large contract on the generators and its related companies' group-level earnings…" in clause 13.271(2)(d).[33]

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[31] See pages 5-7 of Meridian's submission.
[32] See pages 5-6 of Genesis's submission.
[33] See page 6 of Meridian's submission.

Genesis and Mercury considered the disclosure requirements contained in clause 13.271(2)(d) are irrelevant to both the on-selling and "net value" tests.

7.8. Genesis disagrees with 13.271(3)(a)(v) which requires the generator to show the assumptions used for determining the monetary value underpinning the contract are consistent with assumptions being made elsewhere in the generator's business in the 30 business days preceding the date the MLC entered the contract. Genesis argues that "relative to other contracts, MLCs can take time to negotiate and enter and that once certain terms and risk allocations are agreed in principle, these can be difficult to change without damaging the ongoing commercial negotiations… Accordingly,… the assumptions used for a MLC and non-MLC differ and it is unduly onerous for participants to disclose assumption changes for contracts that bear on value as a counterfactual or have any relevance to the MLC (whether because of size, counterparty risk, etc)."[34]

7.9. Meridian note that clause 13.271(2)(c) seeks evidence supporting the generator's reasons given in clause 13.271(2)(b) as to how the MLC satisfies the Code. They consider disclosure requirements in clause 13.271(3) and (4) are unnecessary and overly prescriptive. Meridian considers generators should be free to determine what, if any, additional evidence is relevant to provide to the Authority besides the contract.[35]

7.10. Genesis also proposes that clause 13.271(1)(b) and (c) should be deleted as they impose ongoing and additional obligations to generators where changes to contracts do not affect the MLC tests. Clause 13.271(1)(b) and (c) require generators to disclose changes in materially large contracts which are reasonably likely to result in the net value no longer being positive or affect the onselling arrangements if a generator is relying on a MLC allowing on-selling.[36]

Authority's response

7.11. The Authority considers a requirement to disclose MLCs is more efficient than relying upon the generator's discretion complemented by the Authority's section 46 information powers. The information the Authority anticipates it would require in all cases, to assess compliance with the tests in the proposed Code amendment, can mostly be foreseen and prescribed in advance by the Authority. Prescribing this core information in advance in the Code provides participants with more clarity about what information might be relevant, and avoids the time delay which would be caused if the Authority had to instead rely on section 46 of the Act to gather the information. Prescribing the disclosure requirements also supports a timelier response from the Authority to the compliance or clearance of the MLC, and thereby reduces the period of any commercial uncertainty. In those instances where further information is required beyond that prescribed explicitly in the Code, the Authority would rely on voluntary disclosure by the participant, backed by section 46 powers if the generator declines to provide the information voluntarily.

7.12. The Authority, on balance, agrees with Genesis's proposal to delete the words "or may be" from clauses 13.271(3)(b) and 13.271(4)(b). This amendment limits the "other information" the generator is mandated to disclose to information which it considers to be "material to an assessment", as contrasted with material which is or "may be material to an assessment". The deleted words recognise a potential divergence between what the generator itself considers material and what the generator considers may be material to a third party. Deleting these words from the proposed Code avoids putting the generator in a position where it must "second guess" what may be relevant to a third party, and therefore will reduce the uncertainty and compliance costs they face. Section 46 of the Act can be relied upon in those cases where the Authority deems it necessary, to confirm the existence or not of further information which may be relevant to the Authority's compliance activities.

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[34] See page 5 of Schedule 1 of Genesis's submission.

[35] See pages 6-7 of Meridian's submission.

[36] See page 4 of Schedule 1 of Genesis's submission.

7.13. The Authority agrees with the submission that the information disclosure requirements should be specific to the clause the generator is seeking to rely upon to permit it giving effect to a MLC. However, the proposed Code provides just that. Clause 13.271(3)(a) sets out the disclosure requirements for generators relying on clause 13.269(1)(a) – the "net value" test. Clause 13.271(4) mandates the disclosure requirements for generators relying on clause 13.269(1)(b) – the "on-selling test". The Authority considers the prescribed evidential requirements are appropriate for each of the tests.

7.14. The Authority agrees with the proposal that clause 13.271(2)(d), which sets out disclosure requirements with respect to financial modelling, should be deleted as the information is not directly relevant to determining compliance with the provisions in section 13.269(1)(a) or (b), which allow the giving effect to a MLC. Clause 13.271(2)(d) will be deleted from the finalised Code amendment.

7.15. With respect to 13.271(3)(a)(v), the Authority acknowledges the attributes identified by Genesis as distinctive to MLCs relative to many other contracts, including relative size, counterparty credit risk, and the duration of negotiations. The Authority considers that evidence of assumptions used for pricing contracts, such as other large load contracts, new generation investment business cases, or long term PPAs, can be useful in informing the legitimacy of the counterfactual for assessing the value of the MLC and the best alternative use of electricity (and other resources) supporting an arrangement. Often a direct comparison of the assumptions used to value a MLC and another deal may not be appropriate, but this information can still be used to assist with calibrating relative values.

7.16. The Authority has, however, reconsidered the period of negotiation of MLCs, and on reflection considers a 60-business day (3-month) period preceding the MLC is more appropriate, than the 30 days (6 weeks) originally proposed. Consequently, the Authority has determined to keep clause 13.271(3)(a)(v) unchanged, other than to extend the period it covers to 60 days immediately preceding the date the generator enters the MLC.

7.17. The Authority disagrees with Meridian's suggestion that clauses 13.271(2)(c), or clauses 13.271(3) and (4) are not required. The Authority has elected to keep clause 13.271(3) and (4) as these clauses prescribe the evidence the Authority expects it will require to determine compliance, and it is expedient for this evidence to be prescribed in the Code and not dependent upon generators self-assessing what is required or requiring a section 46 request. Nothing in the Code precludes the generator voluntarily providing additional information.

Simplifying disclosure requirements for contracts which allow on-selling

What the Authority proposed

7.18. The originally proposed clause 13.271 stated the information a generator must provide the Authority under clearance and disclosure regimes. Submitters commented on the following provisions:

(a) Clause 13.271(1)(b) and (c) required a generator to provide information specified in this clause to the Authority in the form and by the means specified by the Authority no later than 5 business days after changing a MLC's price, volume, term or on-selling arrangements or any other provision of a MLC that may affect the calculation of the net value if a generator relies on clause 13.269(1)(a) or changing a MLC's on-selling arrangements if the generator is relying on clause 13.269(1)(b)

(b) Clause 13.271(4)(a) required a generator relying on the on-selling test to provide as part of the evidence in clause 13.271(2)(c) a statement of the buyer's rights to on-sell any un-used MW quantities under the MLC and an explanation of the terms on which it can do so.

(c) Clause 13.271(4)(b) required a generator to disclose all other information and documents that are in the possession of, or under the control, of the generator and that are or may be material to an assessment of a generator's compliance with the on-selling test.

Issue raised by submitters

7.19. Contact submitted that clause 13.271(4) can be simplified. It considered that:

(a) Clause 13.271(4)(a) is unnecessary as there will typically be no terms in a contract allowing on-selling. They propose a clause 13.269(1)(b)(i) "for the avoidance of doubt this requirement can be met by the absence of any clause in the contract prohibiting on-selling of unused MW".

(b) Clause 13.271(4)(b) should be deleted as there are no means for a seller to amend a contract after it is signed, if the buyer enters a back-to-back CFD, or similar contract to on-sell unused MW, or reduce volume purchased on the spot market. In practice, a contract does not require particular terms to allow for on-selling and there is no way for a seller to unilaterally change a contract's terms to then prohibit on-selling once a back to back CFD is set up. Therefore, information to assess compliance is not necessary.[37]

Authority's response

7.20. Contact's position regarding clause 13.271(4)(a) appears to assume on-selling is permitted absent terms in the contract precluding or restricting on-selling, in which case there would be no terms in the contract for which to provide an explanation. However, where there are no clauses in the contract restricting on-selling, then (in addition to providing the contract itself) the generator can comply with clause 13.271(4)(a) by providing a statement which says that there are no restrictions in the contract relating to on-selling and the buyer is free to sell any unused MWs as they choose, without the buyer being subject to any worse terms than if it had consumed the electricity itself. Alternatively, generators could agree to include in future contracts clauses which, for the avoidance of doubt, make it explicit, that buyers are free to on-sell on no worse terms.

7.21. The Authority agrees with Contact that sellers do not have the capacity to unilaterally amend a contract in response to a buyer signing another contract (either with the generating party to the MLC or an independent third party). Clause 13.271(4)(b) requires the generator to provide information, if any, beyond the contract and supporting statement in clause 13.271(4)(a), which is material to the assessment. An example might be correspondence with the buyer confirming their rights to on-sell. Further, as noted above, the Authority has determined to delete the phrase "or may be" from this clause.

[37] See pages 14-15 of Contact's submission.

8. Clearance regime

Clearance regime timeframes and other matters

What the Authority proposed

8.1. The originally proposed Code amendment consulted on provided a 45-business day timeframe for clearance, subject to the generator providing the Authority all the required information.

8.2. Clause 13.273(3) provided that the Authority must make a decision on a clearance application and notify the generator the outcome no later than 45 business days after the date on which the generator has provided the Authority with all required information (including any further information requested by the Authority for the purpose of making its decision), or a longer period as the Authority and the generator agree.

8.3. Clause 13.273(4) provided that if the 45 business days expires without the Authority providing a clearance notice, the Authority shall be deemed to have declined to give a clearance.

8.4. Clause 13.273(7) provided that a clearance on respect of a MLC will expire if the contract is not signed within 20 business days of the Authority providing the clearance.

Issue raised by submitters

8.5. Meridian suggests the clearance for "positive net value" should be completed within 20 working days and clearance for on-selling should be completed within 5 working days. They observe that the Commerce Commission has 40 working days for a business acquisition clearance, and clearance for collaborative activity takes 30 working days.[38]

8.6. Firstgas suggests that the Authority change 45 working days to 'as soon as reasonably practical'.[39]

8.7. Meridian also argues that parties should be able to withdraw an application and, if appropriate, refile at a later date.[40]

8.8. Mercury and Contact note that clauses 13.273(3) and (4) don't provide any certainty regarding the timing of providing a clearance, nor the reasons for not providing a clearance.[41]

8.9. Meridian, Genesis, Mercury and Contact suggest that clause 13.273(4) should be amended so that clearance would be deemed to have been approved if the Authority does not provide notice under subclause (1)(b) within 45 business days.[42]

8.10. Genesis proposes that clause 13.273(7) should extend the period for a cleared contract to be signed before clearance lapses should be extended from 20 business days to 60 business days.[43]

8.11. Vector proposes there should be a mandatory requirement for the Authority to assess and clear or decline all MLCs, and would support requiring all MLCs involving more than one generator on the sell side to be reviewed by the Commerce Commission.[44]

8.12. Meridian suggests the Authority introduces an optional clearance regime where the clearance regime could be extended to allow the Authority discretion to grant clearance

[38] See pages 7-8 of Meridian's submission.
[39] See page 7 of Firstgas's submission.
[40] See page 8 of Meridian's submission.
[41] See pages 16-17 of Contact's submission and page 3 of Mercury's submission.
[42] See page 3 of Mercury's submission, page 17 of Contact's submission, page 7 of Schedule 1 of Genesis's submission, and page 8 of Meridian's submission.
[43] See page 8 of Schedule 1 of Genesis's submission.
[44] See page 1 of Vector's submission.

where the ‘net value’ or ‘on-selling’ tests are not met but the Authority considers the relevant contract is in the long-term interests of consumers. The purpose of an optional clearance regime is to allow for the fact that it is not possible to anticipate the nature of every large contract in the future[45].

Authority’s response

8.13. The Authority set the 45-business day timeframe to notify the generator of its decision reflecting the time it might be expected to complete the analysis and make a decision. This period is not dissimilar to the time-period provided for Commerce Commission merger and acquisition decisions and reflects the complexity of the decision. The Authority considers that 45 business days is not long in the context of the timeframes for negotiating and the materiality of these contracts.

8.14. The Authority is of the view that 45 business days provides more clarity than Firstgas’s suggestion that the timeframes should be changed to ‘as soon as reasonably practical’.

8.15. There is nothing preventing the generator to a MLC from withdrawing a clearance application, and that can be done without specific clauses in the Code. If a generator were to notify the Authority that they were no longer seeking a clearance, then the Authority would cease the process. In this situation the onus would be on the generator to resubmit if, at a later date, they wished to do so.

8.16. The Authority does not consider there is uncertainty in the timeframe for a decision on clearance. Clause 13.273(3) requires the Authority to, within 45 business days, notify the generator of its decision. Clause 13.273(4) provides for the situation where the Authority does not notify the generator in that timeframe, in which case the clearance is deemed to be declined. Clause 13.273(4) provides a backstop in the event the Authority is not able to complete the work within the required timeframe and where the generator will not agree to an extension under clause 13.271(3).

8.17. The Authority considers 20 business days is an appropriate and practical time frame for a cleared contract to be signed by the respective parties. Given the resource intensiveness of the process for clearing MLCs and there is no proposed cost recovery mechanism, generators should be incentivised to only seek clearance for contracts which either have been signed conditional on clearance or are unsigned but have a high level of certainty they will be signed by the parties shortly after clearance is notified.

8.18. The expectation is that the generator and buyer have at least agreed in principle to the terms in the contract which is being assessed by the Authority for clearance. Mandating a relatively short period within which cleared MLCs can be signed is consistent with this incentive. The Authority is also concerned to ensure the period parties have for signing a cleared MLC is not so long that there is significant option value in waiting to see how future electricity prices develop (as forward price volatility has the potential to change the positive net value attributed to the MLC), though these concerns are mitigated where the contract allows on-selling. On balance the Authority considers the 20 business days provided in the proposed Code amendment is appropriate, as the cleared contract should have no surprises to either party to the contract; that parties can anticipate and agree timely processes for signing the contract if clearance is granted; and it doesn’t create the opportunity for significant option value for the parties.

8.19. In response to Vector’s proposals, the Authority is still of the view that a voluntary clearance regime is appropriate. This process allows generators to assess and balance the risks of entering a contract which may subsequently be undone if it is in breach against any additional costs of the clearance regime. The Authority remains free to investigate allegations of Code breaches for an extended period following entry into such a contract.

[45] See page 7 of Meridian’s submission.

The risk of such an investigation (and risk of a breach finding) may itself incentivise parties to use the voluntary clearance regime.

8.20. The obligations in the Code amendment are in addition to obligations in the Commerce Act. Moreover, nothing in the Code amendment affects generators' obligations to comply with the Commerce Act.

8.21. The Authority considers that reliance on the net value and on-selling tests are sufficient to ensure MLCs which are in the interests of consumers will be allowable. It is not necessary to introduce a public interest test in addition to the existing tests and, the Authority is concerned that such a test may in fact create further uncertainty.

Changes to a cleared contract

What the Authority proposed

8.22. The originally proposed clause 13.273(6) stated that clearance does not apply to a MLC if changes are made to the price, volume, term, on-selling arrangements or any other provisions of the MLC that may affect the calculation of the net value or the on-selling arrangements.

8.23. Clause 13.269 defined the restriction on MLCs. A generator must not give effect to a MLC unless –

(a) the net value of the materially large contract to the generator calculated in accordance with clause 13.270 is a positive value; or

(b) the materially large contract allows the buyer to on-sell any un-used MW quantities under the materially large contract without the buyer being subject to any worse terms than if it had consumed the relevant quantity itself; or

(c) the Authority has provided a clearance under clause 13.273 in respect of the materially large contract and that clearance remains effective and applicable.

Issue raised by submitters

8.24. Genesis suggests that the proposed Code amendment invalidates a clearance even if changes made to the contract post-clearance would have strengthened the case for clearance. For example, they suggest the current drafting implies that, in the case of a clearance granted on the basis of clause 13.269(1)(a), even if the change to the contract would result in a higher price than that in the cleared contract, all other terms remaining the same, that a clearance would be invalidated. Similarly, with respect to clearances made on the basis of clause 13.269(1)(b), Genesis suggests the clearance should not apply only if the change "results in the buyer being subject to any worse terms". Genesis propose clause 13.273(6) should be amended so that clearance only falls way if a cleared MLC is amended and the clearance no longer complies with the tests in clauses 13.269(1) and (2).[46]

Authority's response

8.25. The Authority accepts the principle that a clearance should only fall away if a subsequent amendment to the cleared MLC would have had an adverse impact on the applicable test relied upon for granting the clearance. Changes which strengthen the test result (e.g. an increase in the contract price, and all other clauses, such as term and demand response. are unchanged) should not be a basis for undoing a clearance.

8.26. The drafting changes to clause 13.273, proposed by Genesis, provides for situations where any change to the contract weakens the applicable test but would still result in the relevant test being passed e.g. the proposed drafting would allow a clearance to stand where a change reduced the positive result of a test but the result remains positive. For

[46] See page 7 of Schedule 1 of Genesis's submission.

example, in the case of a MLC cleared under clause 13.269(1)(a), the clearance would only be revoked if the net value test ceased to be a positive value.

8.27. While this is the appropriate test conceptually, practically, there may be differences of opinion as to whether the test remains positive after the change in terms. In this circumstance the Authority would need to confirm ongoing compliance itself, and not rely upon a generator's assessment. The proposed approach would necessitate a reassessment by the Authority as to whether the test is indeed still positive.

8.28. The Authority has determined not to change clauses 13.273(6)(a) and (b) but has decided to add a new clause 13.273(6)(c) as outlined above.

8.29. The Code amendment now requires generators to re-disclose contracts only in cases where those changes may affect the net value test (e.g. price, volume, term) if relying on clause 13.269(1)(a) or changes to on-selling arrangements if a generator relies on clause 13.269(1)(b); or where there has been a change to the volume or timing or any new generation taken into account in reliance on clause 13.268(4).

Requirement to publish the outcome of a clearance application

What the Authority proposed

8.30. The originally proposed clause 13.273(5) provided for the Authority to publish the outcome of a clearance application process.

Issue raised by submitters

8.31. Genesis recommends deleting clause 13.273(5), noting the parties are subject to wholesale disclosure information obligations and therefore the relevant disclosures will be made once the MLC is entered into. They suggest publication of the Authority's decision is not required and if published prematurely, may prejudice the commercial interests of the parties.[47]

8.32. However, Vector is of the view that the Authority should publish clearance applications, draft decisions and final decisions with commercially sensitive information redacted where necessary in the same way the Commerce Commission publishes applications for mergers and acquisitions on its website[48].

Authority's response

8.33. The Authority considers the publishing of the outcomes of applications is generally consistent with building public confidence in electricity markets, as well as building a transparent body of understanding of how the Code amendment is being applied. All this can be achieved without publishing commercially sensitive information.

8.34. Clause 13.273(5) provides the Authority with the power to publish the outcome of an application, if it so chooses. The clause is with respect to the "outcome of the application" and does not extend to publishing the contract or other information. Moreover, clause 13.278 requires the Authority to keep confidential all information it receives with respect to the relevant sub-part. Where the disclosure of the parties to a proposed MLC would prejudice the commercial interests of the parties, say where the contract has yet to be entered into, clause 13.278 would provide the necessary protections.

8.35. The Authority does not consider it is appropriate to mandate in the Code a requirement that it publish applications or draft decisions because, for example, the fact two parties are in a negotiation could be commercially sensitive in itself.

[47] See page 7 of Schedule 1 of Genesis's submission.
[48] See page 6 of Vector's submission.

Rulings Panel should be able to direct the Authority

What the Authority proposed

8.36. The originally proposed clause 13.275(4) stated the Rulings Panel, in determining an appeal, must either approve the decision the Authority or direct the Authority to reconsider the decision in full or by reference to specified matters.

Issue raised by submitters

8.37. Genesis suggest the Ruling Panel should be able to direct the Authority to provide clearance or reconsider the decision in full or on specific matters. The Authority should not have any ability to fetter the Panel's powers, rather the Panel should be able to direct the Authority.[49]

Authority's response

8.38. Section 61 of the Act states that when determining an appeal, the Rulings Panel can make any direction it sees fit, subject to any provisions in the Code relating to that appeal. So in this case, the Rulings Panel can make a direction subject to what clause 13.275(4) says. Clause 13.275(4) says that the Rulings Panel can either approve the decision or direct the Authority to reconsider the decision. Therefore, the Rulings Panel does not have the ability to grant clearance. It is the Authority that has the resources to carry out the analysis required to determine whether a MLC is efficient and hence provide clearance. Accordingly, the Authority is comfortable with this clause as drafted

9. Next steps

9.1. In light of the permanent amendment to the Code, the Authority considers that the continued application of the urgent Code is not required, as the circumstances it was designed to address no longer exist. Therefore, on 19 May 2023 the Code amendment will become effective and the urgent Code will be revoked.

9.2. As discussed above, the Authority will monitor clause 13.268(1)(a) – (c) and could refine clause 13.268(1)(c) in the event of generators disclosing contract(s) which the Authority considers not to be materially large contracts. A future change may be warranted if the current clauses are imposing unreasonable compliance costs on generators, and the public policy interest can be achieved more efficiently.

9.3. The Authority will also consider publishing a guidance note, explaining the working of the amendment to clause 13.268(1)(a)(ii) which will include types of contracts which are and are not covered by the clause.

Attachments

The following appendices are attached to this paper:

- Appendix A Code Amendment
- Appendix B Code Amendment (track changes)

[49] See page 8 of Schedule 1 of Genesis's submission.

Appendix A Code Amendment

Location of new Code amendment: Part 13, new subpart 7

"**13.267 Contents of this subpart**

"This subpart provides for—

"(a) restrictions on giving effect to **materially large contracts**; and

"(b) information disclosure requirements to support compliance with this subpart; and

"(c) a clearance regime for **materially large contracts**.

"**13.268 Definition of materially large contract**

"(1) A **materially large contract** is—

"(a) a contract that—

"(i) is not entered into through a derivatives exchange; and

"(ii) includes terms under which the **buyer** itself will consume electricity ; and

"(iii) relates to a net quantity of **electricity** that equals or exceeds 150 **MW** consumed at a point in time; or

"(b) two or more contracts where:

"(i) all the contracts satisfy paragraph (a)(i); and

"(ii) at least one contract satisfies paragraph (a)(ii); and

"(iii) the contracts when taken together satisfy paragraph (a)(iii) and meet one of the descriptions set out in paragraph (c) below:

"(c) the descriptions referred to at paragraph (b)(iii) above are:

"(i) two or more contracts between a **generator** and a **buyer**; or

"(ii) at least one contract between a **generator** and a **buyer** and at least one contract between that **generator** or its related company and that **buyer** or its related company; or

"(iii) at least one contract between a **generator** and a **buyer** and at least one contract involving a second **generator** and the same **buyer** where the contracts rely on each other or are otherwise interdependent ; or

"(iv) at least one contract between a **generator** and a **buyer** and at least one contract between the same generator and a second **generator** where the contracts rely on each other or are otherwise interdependent; or

"(v) any other arrangement that is substantially of the same kind as that described in any of subparagraphs (i)-(iv).

"(2) For **materially large contracts** made up of two or more different **generators'** contracts, any reference to **materially large contract** in the following clauses must be read as only referring to an individual **generator's** contract(s) that forms part of a **materially large contract**, rather than as a reference to the multiple **generators'** contracts.

"(3) Where a **materially large contract** allows for the possibility of varying quantities of **electricity** consumption at any one time, the maximum quantity of **electricity** consumption possible under the contract at any one time is to be used for the purpose of determining whether the **MW** threshold in subclause (1)(a)(iii) is met.

"(4) For the purpose of subclause (1)(a)(iii), the net quantity of **electricity** is the total **MW** consumed at a point in time (calculated in accordance with subclause (3)) less any **MW** generated from new generation, where the materially large contract is material to the generator's decision to invest in the new generation.

"(5) For the purpose of this subpart, related company has the meaning set out in section 2(3) of the Companies Act 1993.

"**13.269 Restriction on materially large contracts**

"(1) A **generator** must not give effect to a **materially large contract** unless—

"(a) the net value of the **materially large contract** to the **generator** calculated in accordance with clause 13.270 is a positive value; or

"(b) the **materially large contract** allows the **buyer** to on-sell all un-used **MW** quantities under the **materially large contract** without the **buyer** being subject to any worse terms than if it had consumed the relevant quantity itself; or

"(c) the **Authority** has provided a clearance under clause 13.273 in respect of the **materially large contract** and that clearance remains effective and applicable.

"(2) Nothing in this clause prevents a **generator** entering into a **materially large contract** that provides that it is conditional on the **Authority** providing a clearance under clause 13.273.

"(3) This clause only applies to **materially large contracts** entered into, extended or modified on or after the date this clause came into force.

"13.270 Calculation of net value of the materially large contract to the generator

"(1) The net value of the **materially large contract** to the **generator** is the value of the contract to the **generator** less the value of the **generator's** best alternative.

"(2) The calculation of the value of the **generator's** best alternative must take into account the **generator's** reasonable expectations as to whether in the absence of the **materially large contract** the **buyer** would have exited completely, reduced consumption, not expanded, or not entered the domestic market.

"(3) The calculation of the value of the contract to the **generator** and the calculation of the value of the **generator's** best alternative must take into account any direct value components that are reasonably relevant to the calculation, which may include (without limitation)—

"(a) contract price:

"(b) prices for baseload futures contracts over the period covered by the **materially large contract** and, where a **materially large contract** covers a period in time not yet covered by base load futures contracts, the **generator's** reasonable expectations as to base forward prices over this period, which may include consideration of the long run marginal cost of electricity, the levelised cost of electricity and other factors:

"(c) node location:

"(d) load profile differing from base load:
"(e) demand response provisions:
"(f) price separation provisions:
"(g) contract price pegged to an index provision:
"(h) value of maintaining an uninterrupted commercial relationship with the **buyer**:
"(i) relative counterparty risk:
"(j) any other financial inducements or benefits associated with the **materially large contract**.

"(4) For the avoidance of doubt, indirect effects of the **materially large contract** on the **generator's** wider portfolio (for example, revenues from other customers) must not be taken into account when calculating the value of the contract to the **generator** and the value of the **generator's** best alternative.

"(5) Each value component used under subclause (3) must be assigned a monetary value that reasonably equates to its value to the **generator**.

"(6) Each assigned monetary value for a value component must be aggregated to derive the value of the contract to the **generator** and the value of the **generator's** best alternative (as applicable).

"(7) The relevant point in time at which the **generator's** reasonable expectations at subclause (2) and any assumptions relied on under subclause (3) are to be assessed is the duration of the 30 **business days** immediately preceding the **generator** (as applicable)—
"(a) entering into the **materially large contract**; or
"(b) seeking a clearance from the **Authority** for the **materially large contract**.

"13.271 Disclosure of materially large contracts

"(1) Except where clause 13.276 applies, a **generator** must provide the information specified in this clause to the **Authority** in the form and by the means specified by the **Authority** no later than 5 **business days** after—
"(a) entering into a **materially large contract**:
"(b) changing a **materially large contract's** price, volume, term or on-selling arrangements or any other provision of a **materially large contract** that may affect the calculation of the net value of the **materially large contract** to the **generator** if the **generator** is relying on clause 13.269(1)(a) to give effect to the **materially large contract**:
"(c) changing a **materially large contract's** on-selling arrangements if the **generator** is relying on clause 13.269(1)(b) to give effect to the **materially large contract**:
"(d) a change to the volume or timing of any new generation taken into account in reliance on clause 13.268(4) where:
"(i) the quantity of electricity generated from new generation has decreased; and
"(ii) the net quantity of electricity for any contract exceeds the threshold in clause 13.268(1)(a)(iii).

"(2) The information to be provided must consist of the following in relation to the **materially large contract**:
"(a) a copy of the **materially large contract** signed by the **parties**; and

"(b) a statement of the **generator's** reasons as to how the **materially large contract** satisfies either clause 13.269(1)(a) or clause 13.269(1)(b); and

"(c) evidence to support the **generator's** reasons at paragraph (b).

"(3) Where a **generator** seeks to rely on clause 13.269(1)(a), the evidence under subclause (2)(c) must include—

"(a) the **generator's** calculation of the net value of the **materially large contract** to the **generator** in accordance with clause 13.270, including—

"(i) the **generator's** calculation of the value of the contract to the **generator** and the **generator's** best alternative in accordance with clause 13.270; and

"(ii) the value component(s) taken into account by the **generator** when calculating the value of the contract to the **generator**; and

"(iii) the value component(s) taken into account by the **generator** when calculating the value of the **generator's** best alternative; and

"(iv) the monetary value assigned to any value component taken into account by the **generator**; and

"(v) a justification for the monetary value assigned to any value component, including any assumptions relied on and (if available) evidence to show whether those assumptions are consistent with similar assumptions being made elsewhere in the **generator's** business in the 60 **business days** immediately preceding the date the **generator** entered into the **materially large contract**; and

"(vi) the **generator's** reasonable expectations taken into account under clause 13.270(2) and an explanation of the basis for these expectations and (if available) evidence to support those expectations; and

"(b) all other information and documents that are in the possession, or under the control, of the **generator** and that are material to an assessment of a **generator's** compliance with clause 13.269(1)(a).

"(4) Where a **generator** seeks to rely on clause 13.269(1)(b), the evidence under subclause (2)(c) must include—

"(a) a statement of the **buyer**'s rights to on-sell any un-used **MW** quantities under the **materially large contract** and an explanation of the terms on which it can do so; and

"(b) all other information and documents that are in the possession, or under the control, of the **generator** and that are material to an assessment of a **generator's** compliance with clause 13.269(1)(b).

"**13.272 Application to the Authority for clearance of a materially large contract**

"(1) A **generator** may submit an application to the **Authority** for clearance of a **materially large contract** that—

"(a) is expressed as conditional on the **Authority** providing a clearance under this subpart; or

"(b) has not yet been signed by the **parties**.

"(2) Where a **generator** has not provided the information specified at clause 13.271 in respect of the **materially large contract** the application must include all

information specified in clause 13.271 that would otherwise be required to be provided by the **generator** after entering the **materially large contract**.

"(3) The application must be submitted in the form and by the means specified by the **Authority**.

"**13.273 Authority may provide clearance for a materially large contract**

"(1) Where the **Authority** receives an application that complies with clause 13.272 the **Authority** shall either—

"(a) provide a clearance by notice in writing in respect of the **materially large contract** if it is satisfied that either clause 13.269(1)(a) or 13.269(1)(b) is met, in which case the Authority must specify which clause it is satisfied in respect of; or

"(b) decline by notice in writing to provide a clearance in respect of the **materially large contract** if it is not satisfied that either clause 13.269(1)(a) or 13.269(1)(b) is met, in which case the **Authority** must give the **generator** reasons for its decision.

"(2) The **Authority** may use the information provided to it in the application and any other information the **Authority** considers relevant for the purposes of its decision, including any further information the Authority requests from the **generator**.

"(3) The **Authority** must make a decision on the application and notify the **generator** of the outcome of its application no later than 45 **business days** after the date on which the **generator** has provided the **Authority** with all required information (including any further information requested by the **Authority** for the purpose of making its decision), or such longer period as the **Authority** and the **generator** agree.

"(4) If the period specified in subclause (3) expires without the **Authority** having provided a clearance for the **materially large contract** and without having given a notice under subclause (1)(b), the **Authority** shall be deemed to have declined to give a clearance.

"(5) The **Authority** may publish the outcome of the application.

"(6) A clearance provided by the **Authority** under this clause does not apply to a **materially large contract** if—

"(a) any changes are made to the price, volume, term, on-selling arrangements or any other provision of the **materially large contract** that may affect the calculation of the net value of the **materially large contract** to the **generator** and the **Authority** provided its clearance on the basis of clause 13.269(1)(a); or

"(b) any changes are made to the **materially large contract's** on-selling arrangements and the **Authority** provided its clearance on the basis of clause 13.269(1)(b); or

"(c) there has been a change to the volume or timing of any new generation taken into account in reliance on clause 13.268(4) where:

"(i) the quantity of electricity generated from new generation has decreased; and

"(ii) the net quantity of electricity for any contract exceeds the threshold in clause 13.268(1)(a)(iii).

"(7) Where the **Authority** provides a clearance in respect of a **materially large contract** not yet signed by the **parties**, the clearance will expire and be of no effect if the contract is not signed by the **parties** within 20 **business days** of the **Authority** providing the clearance.

"(8) The **Authority** may revoke a clearance if it was based on information provided by the **generator** that was false or misleading in a material particular.

"13.274 Reconsideration by Authority of clearance decision

"(1) Where the **Authority** declines to provide a clearance, the **Authority** may, at its discretion, reconsider its decision if—

"(a) the **generator** provides further information or reasons (which may include making changes to the **materially large contract**) to the **Authority** in support of its position no later than 10 **business days** after notification of the **Authority's** decision under clause 13.273; and

"(b) the **Authority** considers that the further information or reasons may alter or affect the **Authority's** decision under clause 13.273.

"(2) The **Authority** must make any decisions under this clause within such timeframes as it reasonably considers appropriate.

"**13.275 Right of appeal against clearance decision**

"(1) A party to a **materially large contract** may appeal to the **Rulings Panel** a decision by the **Authority** under clause 13.273 not to provide a clearance in respect of the **materially large contract**.

"(2) Despite subclause (1) a party to a **materially large contract** may not appeal to the **Rulings Panel** where the reason for the decision not to provide clearance relates to a failure by the **generator** to provide required information.

"(3) The appeal must be made to the **Rulings Panel** no later than 20 **business days** after the **Authority** notifies the **generator** of its decision under clause 13.273.

"(4) The **Rulings Panel**, in determining an appeal, must either approve the decision of the **Authority** or direct the **Authority** to reconsider the decision in full or by reference to specified matters.

"**13.276 Disclosure of cleared materially large contract**

"(1) This clause applies to a **materially large contract** that has been provided with a clearance under clause 13.273 provided the clearance remains effective and applicable.

"(2) Where this clause applies, a **generator** must provide to the **Authority** a copy of the **materially large contract** signed by the **parties** in the form and by the means specified by the **Authority** no later than 5 **business days** after entering into the **materially large contract**.

"**13.277 Requirement to provide complete and accurate information**

"(1) In addition to the requirements of clause 13.2, the **generator** must take all practicable steps to ensure that the information that the **generator** is required to provide under this subpart is complete and accurate as at the date it is required to be provided under this subpart.

"(2) If the **generator** later becomes aware that any information provided under this subpart was not complete or accurate as at the date it was required to be provided under this subpart, it must as soon as practicable provide to the **Authority** such further information as is necessary to make the information complete or accurate as at the date it was required to be provided under this subpart.

"**13.278 Authority must keep information confidential**

The **Authority** must keep all information provided to it under this subpart confidential except to the extent that disclosure is required to enable the **Authority** to carry out its obligations and duties under the Electricity Industry Act 2010, the Code or the Electricity Industry (Enforcement) Regulations or is otherwise required by law.

"**13.279 Appointment of auditor**

"(1) The **Authority** may, in its discretion, carry out an audit as to whether a **generator** has complied with this subpart.

"(2) If the **Authority** decides under subclause (1) that a **generator** should be subject to an audit—

"(a) the **Authority** must require the **generator** to nominate an appropriate auditor; and

"(b) the **generator** must provide that nomination to the **Authority** within a reasonable timeframe.

"(3) The **Authority** may appoint the auditor nominated by the **generator** or a different auditor, having regard to any factors it considers relevant in the circumstances, including—

"(a) the expected quality of the audit:

"(b) the expected costs of the audit.

"(4) If the **generator** fails to nominate an appropriate auditor within 20 **business days**, the **Authority** may appoint an auditor of its own choice.

"**13.280 Carrying out of audit**

"(1) A **generator** subject to an audit under clause 13.279 must, on request from the auditor, provide the auditor with such information as the auditor reasonably requires in order to carry out the audit.

"(2) The **generator** must provide the information no later than 20 **business days** after receiving a request from the auditor for the information.

"(3) The **generator** must ensure that the auditor provides the **Authority** with an audit report on the **generator**'s compliance with this subpart within the timeframe specified by the **Authority**.

"(4) The audit report must include any other information the **Authority** may reasonably require.

"(5) Before the audit report is provided to the **Authority**, any identified failure of the **generator** to comply with this subpart must be referred back to the **generator** for comment.

"(6) The comments of the **generator** must be included in the audit report.

"(7) The audit report must not contain any contract that the **generator** has provided to the auditor unless the contract meets the definition of a **materially large contract**.

"**13.281 Payment of costs relating to audits**

"(1) If an audit establishes, to the reasonable satisfaction of the **Authority**, that a **generator** may not have complied with this subpart (whether or not the **Authority** appoints an investigator to investigate the alleged breach), the **generator** must pay for the audit.

"(2) If the **Authority** considers that the non-compliance of the **generator** is minor or there is any other reason in the Authority's view that means the **generator** should not pay the costs of the audit, the **Authority** may, in its discretion, determine the proportion of the costs of the audit that are to be paid by the **generator**, and those costs must be paid by the **generator** with any remaining proportion of costs paid by the **Authority**.

"(3) If an audit establishes to the reasonable satisfaction of the **Authority** that the **generator** has complied with this subpart, the **generator** is not required to pay any of the auditor's costs and the **Authority** will pay the auditor's costs."

"13.282 Transitional arrangements

"(1) Where:

"(a) an application has been made to the **Authority** for clearance of a **materially large contract** pursuant to clause 13.272 prior to 19 May 2023; and

"(b) as at 19 May 2023:

"(i) the **Authority** has not yet made a decision on the application and notified the **generator** of the outcome; and

"(ii) the period specified in clause 13.272(3) has either:

"(A) not yet expired; or

"(B) has been extended by agreement between the **Authority** and the **generator**;

then, the **Authority** shall make a decision on the application as if this subpart, as it existed on 18 May 2023, continued in force.

"(2) Once the Authority has made a decision on an application to which subclause (1) applies, the matters and arrangements which were subject of the application shall be dealt with in accordance with this subpart.

"(3) Where:

"(a) an application has been made to the **Authority** for clearance of a **materially large contract** pursuant to clause 13.272 prior to 19 May 2023; and

"(b) the **Authority** has, pursuant to clause 13.273(1)(a), provided a clearance by notice in writing prior to 19 May 2023;

then, the **materially large contract** and the matters and arrangements which were subject of the application, shall be dealt with in accordance with this subpart.

Appendix B Code Amendment (track changes)

Location of new Code amendment: Part 13, new subpart 7

"**13.267 Contents of this subpart**

"This subpart provides for—

"(a) restrictions on giving effect to **materially large contracts**; and

"(b) information disclosure requirements to support compliance with this subpart; and

"(c) a clearance regime for **materially large contracts**.

"**13.268 Definition of materially large contract**

"(1) A **materially large contract** is—

"(a) a contract that—

"(i) is not entered into through a derivatives exchange; and

"(ii) includes terms under which the **buyer** itself will consume electricity ~~relates to the physical consumption of **electricity**~~; and

"(iii) relates to a net quantity of **electricity** that equals or exceeds 150 **MW** consumed at a point in time; or

"(b) two or more contracts where:

"(i) all the contracts satisfy paragraph (a)(i); and

"(ii) at least one contract~~-~~ satisfies~~y~~ paragraph (a)~~(i)~~ (ii); and

"(iii) the contracts when taken together satisfy paragraph (a)(iii) and meet one of the ~~following~~ descriptions set out in paragraph (c) below:

"(c) the descriptions referred to at paragraph (b)(iii) above are:

"(i) two or more contracts between a **generator** and a **buyer**; or

"(ii) at least one contract between a **generator** and a **buyer** and at least one contract between that **generator** or its related company and that **buyer** or its related company; or

"(iii) at least one contract between a **generator** and a **buyer** and at least one contract involving a second **generator** and the same **buyer** where the contracts rely on each other or are otherwise interdependent ~~at least one contract between a **generator** and a **buyer** and at least one contract involving a second **generator** where the contracts rely on each other or are otherwise interdependent~~; or

"(iv) at least one contract between a **generator** and a **buyer** and at least one contract between the same generator and a second **generator** where the contracts rely on each other or are otherwise interdependent; or~~.~~

"(~~i~~v) any other arrangement that is substantially of the same kind as that described in any of subparagraphs (i)-(~~iii~~iv).

"(2) For **materially large contracts** made up of two or more different **generators'** contracts, any reference to **materially large contract** in the following clauses must be read as only referring to an individual **generator's** contract(s) that forms part of

a **materially large contract**, rather than as a reference to the multiple **generators'** contracts.

"(3) Where a **materially large contract** allows for the possibility of varying quantities of **electricity** consumption at any one time, the maximum quantity of **electricity** consumption possible under the contract at any one time is to be used for the purpose of determining whether the **MW** threshold in subclause (1)(a)(iii) is met.

"(4) For the purpose of subclause (1)(a)(iii), the net quantity of **electricity** is the total **MW** consumed at a point in time (calculated in accordance with subclause (3)) less any **MW** generated ~~consumed~~ from new generation, where the materially large contract is material to the generator's decision to invest in the new generation. ~~built as a consequence of the contract.~~

"(5) For the purpose of this subpart, related company has the meaning set out in section 2(3) of the Companies Act 1993.

"**13.269 Restriction on materially large contracts**

"(1) A **generator** must not give effect to a **materially large contract** unless—

"(a) the net value of the **materially large contract** to the **generator** calculated in accordance with clause 13.270 is a positive value; or

"(b) the **materially large contract** allows the **buyer** to on-sell all~~any~~ un-used **MW** quantities under the **materially large contract** without the **buyer** being subject to any worse terms than if it had consumed the relevant quantity itself; or

"(c) the **Authority** has provided a clearance under clause 13.273 in respect of the **materially large contract** and that clearance remains effective and applicable.

"(2) Nothing in this clause prevents a **generator** entering into a **materially large contract** that provides that it is conditional on the **Authority** providing a clearance under clause 13.273.

"(3) This clause only applies to **materially large contracts** entered into, extended or modified on or after the date this clause came into force.

"**13.270 Calculation of net value of the materially large contract to the generator**

"(1) The net value of the **materially large contract** to the **generator** is the value of the contract to the **generator** less the value of the **generator's** best alternative.

"(2) The calculation of the value of the **generator's** best alternative must take into account the **generator's** reasonable expectations as to whether in the absence of the **materially large contract** the **buyer** would have exited completely, reduced consumption, not expanded, or not entered the domestic market.

"(3) The calculation of the value of the contract to the **generator** and the calculation of the value of the **generator's** best alternative must take into account any direct value components that are reasonably relevant to the calculation, which may include (without limitation)—

"(a) contract price:

"(b) prices for baseload futures contracts over the period covered by the **materially large contract** and, where a **materially large contract** covers a period in time not yet covered by base load futures contracts, the **generator's** reasonable expectations as to base forward prices over this

period, which may include consideration of the long run marginal cost of electricity, the levelised cost of electricity and other factors:

"(c) node location:

"(d) load profile differing from base load:

"(e) demand response provisions:

"(f) price separation provisions:

"(g) contract price pegged to an index provision:

"(h) value of maintaining an uninterrupted commercial relationship with the **buyer**:

"(i) relative counterparty risk:

"(j) any other financial inducements or benefits associated with the **materially large contract**.

"(4) For the avoidance of doubt, indirect effects of the **materially large contract** on the **generator's** wider portfolio (for example, revenues from other customers) must not be taken into account when calculating the value of the contract to the **generator** and the value of the **generator's** best alternative.

"(5) Each value component used under subclause (3) must be assigned a monetary value that reasonably equates to its value to the **generator**.

"(6) Each assigned monetary value for a value component must be aggregated to derive the value of the contract to the **generator** and the value of the **generator's** best alternative (as applicable).

"(7) The relevant point in time at which the **generator's** reasonable expectations at subclause (2) and any assumptions relied on under subclause (3) are to be assessed is the duration of the 30 **business days** immediately preceding the **generator** (as applicable)—

"(a) entering into the **materially large contract**; or

"(b) seeking a clearance from the **Authority** for the **materially large contract**.

"13.271 Disclosure of materially large contracts

"(1) Except where clause 13.276 applies, a **generator** must provide the information specified in this clause to the **Authority** in the form and by the means specified by the **Authority** no later than 5 **business days** after—

"(a) entering into a **materially large contract**:

"(b) changing a **materially large contract's** price, volume, term or ~~re~~on-selling arrangements or any other provision of a **materially large contract** that may affect the calculation of the net value of the **materially large contract** to the **generator** if the **generator** is relying on clause 13.269(1)(a) to give effect to the **materially large contract**:

"(c) changing a **materially large contract's** ~~re~~on-selling arrangements if the **generator** is relying on clause 13.269(1)(b) to give effect to the **materially large contract**: ~~.~~

"(d) a change to the volume or timing of any new generation taken into account in reliance on clause 13.268(4) where:

"(ii) the quantity of electricity generated from new generation has decreased; and

"(ii) the net quantity of electricity for any contract exceeds the threshold in clause 13.268(1)(a)(iii).

"(2) The information to be provided must consist of the following in relation to the **materially large contract**:

"(a) a copy of the **materially large contract** signed by the **parties**; and

"(b) a statement of the **generator's** reasons as to how the **materially large contract** satisfies either clause 13.269(1)(a) or clause 13.269(1)(b); and

"(c) evidence to support the **generator's** reasons at paragraph (b).; and

"(d) any information or documents, including any financial modelling, that are in the possession, or under the control, of the **generator** that discuss or show the impact of the **materially large contract** on the **generator's** and its related companies' group-level earnings before interest, taxes, depreciation, amortisation and fair value adjustments or on the **generator's** and its related companies' broader financial performance and strength.

"(3) Where a **generator** seeks to rely on clause 13.269(1)(a), the evidence under subclause (2)(c) must include—

"(a) the **generator's** calculation of the net value of the **materially large contract** to the **generator** in accordance with clause 13.270, including—

"(i) the **generator's** calculation of the value of the contract to the **generator** and the **generator's** best alternative in accordance with clause 13.270; and

"(ii) the value component(s) taken into account by the **generator** when calculating the value of the contract to the **generator**; and

"(iii) the value component(s) taken into account by the **generator** when calculating the value of the **generator's** best alternative; and

"(iv) the monetary value assigned to any value component taken into account by the **generator**; and

"(v) a justification for the monetary value assigned to any value component, including any assumptions relied on and (if available) evidence to show whether those assumptions are consistent with similar assumptions being made elsewhere in the **generator's** business in the 630 **business days** immediately preceding the date the **generator** entered into the **materially large contract**; and

"(vi) the **generator's** reasonable expectations taken into account under clause 13.270(2) and an explanation of the basis for these expectations and (if available) evidence to support those expectations; and

"(b) all other information and documents that are in the possession, or under the control, of the **generator** and that are or may be material to an assessment of a **generator's** compliance with clause 13.269(1)(a).

"(4) Where a **generator** seeks to rely on clause 13.269(1)(b), the evidence under subclause (2)(c) must include—

"(a) a statement of the **buyer**'s rights to on-sell any un-used **MW** quantities under the **materially large contract** and an explanation of the terms on which it can do so; and

"(b) all other information and documents that are in the possession, or under the control, of the **generator** and that are ~~or may be~~ material to an assessment of a **generator's** compliance with clause 13.269(1)(b).

"**13.272 Application to the Authority for clearance of a materially large contract**

"(1) A **generator** may submit an application to the **Authority** for clearance of a **materially large contract** that—

"(a) is expressed as conditional on the **Authority** providing a clearance under this subpart; or

"(b) has not yet been signed by the **parties**.

"(2) Where a **generator** has not provided the information specified at clause 13.271 in respect of the **materially large contract** the application must include all information specified in clause 13.271 that would otherwise be required to be provided by the **generator** after entering the **materially large contract**.

"(3) The application must be submitted in the form and by the means specified by the **Authority**.

"**13.273 Authority may provide clearance for a materially large contract**

"(1) Where the **Authority** receives an application that complies with clause 13.272 the **Authority** shall either—

"(a) provide a clearance by notice in writing in respect of the **materially large contract** if it is satisfied that either clause 13.269(1)(a) or 13.269(1)(b) is met, in which case the Authority must specify which clause it is satisfied in respect of; or

"(b) decline by notice in writing to provide a clearance in respect of the **materially large contract** if it is not satisfied that either clause 13.269(1)(a) or 13.269(1)(b) is met, in which case the **Authority** must give the **generator** reasons for its decision.

"(2) The **Authority** may use the information provided to it in the application and any other information the **Authority** considers relevant for the purposes of its decision, including any further information the Authority request~~ed~~s from the **generator**.

"(3) The **Authority** must make a decision on the application and notify the **generator** of the outcome of its application no later than 45 **business days** after the date on which the **generator** has provided the **Authority** with all required information (including any further information requested by the **Authority** for the purpose of making its decision), or such longer period as the **Authority** and- the **generator** agree.

"(4) If the period specified in subclause (3) expires without the **Authority** having provided a clearance for the **materially large contract** and without having given a notice under subclause (1)(b), the **Authority** shall be deemed to have declined to give a clearance.

"(5) The **Authority** may publish the outcome of the application.

"(6) A clearance provided by the **Authority** under this clause does not apply to a **materially large contract** if—

"(a) any changes are made to the price, volume, term, on~~re~~-selling arrangements or any other provision of the **materially large contract** that may affect the calculation of the net value of the **materially large contract**

to the **generator** and the **Authority** provided its clearance on the basis of clause 13.269(1)(a); or

"(b) any changes are made to the **materially large contract's** on~~re~~-selling arrangements and the **Authority** provided its clearance on the basis of clause 13.269(1)(b); or~~.~~

"(c) there has been a change to the volume or timing of any new generation taken into account in reliance on clause 13.268(4) where:

"(i) the quantity of electricity generated from new generation has decreased; and

"(ii) the net quantity of electricity for any contract exceeds the threshold in clause 13.268(1)(a)(iii).

"(7) Where the **Authority** provides a clearance in respect of a **materially large contract** not yet signed by the **parties**, the clearance will expire and be of no effect if the contract is not signed by the **parties** within 20 **business days** of the **Authority** providing the clearance.

"(8) The **Authority** may revoke a clearance if it was based on information provided by the **generator** that was false or misleading in a material particular.

"13.274 Reconsideration by Authority of clearance decision

"(1) Where the **Authority** declines to provide a clearance, the **Authority** may, at its discretion, reconsider its decision if—

"(a) the **generator** provides further information or reasons (which may include making changes to the **materially large contract**) to the **Authority** in support of its position no later than 10 **business days** after notification of the **Authority's** decision under clause 13.273; and

"(b) the **Authority** considers that the further information or reasons may alter or affect the **Authority's** decision under clause 13.273.

"(2) The **Authority** must make any decisions under this clause within such timeframes as it reasonably considers appropriate.

"**13.275 Right of appeal against clearance decision**

"(1) A party to a **materially large contract** may appeal to the **Rulings Panel** a decision by the **Authority** under clause 13.273 not to provide a clearance in respect of the **materially large contract**.

"(2) Despite subclause (1) a party to a **materially large contract** may not appeal to the **Rulings Panel** where the reason for the decision not to provide clearance relates to a failure by the **generator** to provide required information.

"(3) The appeal must be made to the **Rulings Panel** no later than 20 **business days** after the **Authority** notifies the **generator** of its decision under clause 13.273.

"(4) The **Rulings Panel**, in determining an appeal, must either approve the decision of the **Authority** or direct the **Authority** to reconsider the decision in full or by reference to specified matters.

"**13.276 Disclosure of cleared materially large contract**

"(1) This clause applies to a **materially large contract** that has been provided with a clearance under clause 13.273 provided the clearance remains effective and applicable.

"(2) Where this clause applies, a **generator** must provide to the **Authority** a copy of the **materially large contract** signed by the **parties** in the form and by the means specified by the **Authority** no later than 5 **business days** after entering into the **materially large contract**.

"**13.277 Requirement to provide complete and accurate information**

"(1) In addition to the requirements of clause 13.2, the **generator** must take all practicable steps to ensure that the information that the **generator** is required to provide under this subpart is complete and accurate as at the date it is required to be provided under this subpart.

"(2) If the **generator** later becomes aware that any information provided under this subpart was not complete or accurate as at the date it was required to be provided under this subpart, it must as soon as practicable provide to the **Authority** such further information as is necessary to make the information complete or accurate as at the date it was required to be provided under this subpart.

"**13.278 Authority must keep information confidential**

The **Authority** must keep all information provided to it under this subpart confidential except to the extent that disclosure is required to enable the **Authority** to carry out its obligations and duties under the Electricity Industry Act 2010, the Code or the Electricity Industry (Enforcement) Regulations or is otherwise required by law.

"**13.279 Appointment of auditor**

"(1) The **Authority** may, in its discretion, carry out an audit as to whether a **generator** has complied with this subpart.

"(2) If the **Authority** decides under subclause (1) that a **generator** should be subject to an audit—

"(a) the **Authority** must require the **generator** to nominate an appropriate auditor; and

"(b) the **generator** must provide that nomination to the **Authority** within a reasonable timeframe.

"(3) The **Authority** may appoint the auditor nominated by the **generator** or a different auditor, having regard to any factors it considers relevant in the circumstances, including—

"(a) the expected quality of the audit:

"(b) the expected costs of the audit.

"(4) If the **generator** fails to nominate an appropriate auditor within 20 **business days**, the **Authority** may appoint an auditor of its own choice.

"**13.280 Carrying out of audit**

"(1) A **generator** subject to an audit under clause 13.279 must, on request from the auditor, provide the auditor with such information as the auditor reasonably requires in order to carry out the audit.

"(2) The **generator** must provide the information no later than 20 **business days** after receiving a request from the auditor for the information.

"(3) The **generator** must ensure that the auditor provides the **Authority** with an audit report on the **generator**'s compliance with this subpart within the timeframe specified by the **Authority**.

"(4) The audit report must include any other information the **Authority** may reasonably require.

"(5) Before the audit report is provided to the **Authority**, any identified failure of the **generator** to comply with this subpart must be referred back to the **generator** for comment.

"(6) The comments of the **generator** must be included in the audit report.

"(7) The audit report must not contain any contract that the **generator** has provided to the auditor unless the contract meets the definition of a **materially large contract**.

"**13.281 Payment of costs relating to audits**

"(1) If an audit establishes, to the reasonable satisfaction of the **Authority**, that a **generator** may not have complied with this subpart (whether or not the **Authority** appoints an investigator to investigate the alleged breach), the **generator** must pay for the audit.

"(2) If the **Authority** considers that the non-compliance of the **generator** is minor or there is any other reason in the Authority's view that means the **generator** should not pay the costs of the audit, the **Authority** may, in its discretion, determine the proportion of the costs of the audit that are to be paid by the **generator**, and those costs must be paid by the **generator** with any remaining proportion of costs paid by the **Authority**.

"(3) If an audit establishes to the reasonable satisfaction of the **Authority** that the **generator** has complied with this subpart, the **generator** is not required to pay any of the auditor's costs and the **Authority** will pay the auditor's costs."

"13.282 Transitional arrangements

"(1) Where:

"(a) an application has been made to the **Authority** for clearance of a **materially large contract** pursuant to clause 13.272 prior to 19 May 2023; and

"(b) as at 19 May 2023:

"(i) the **Authority** has not yet made a decision on the application and notified the **generator** of the outcome; and

"(ii) the period specified in clause 13.272(3) has either:

"(A) not yet expired; or

"(B) has been extended by agreement between the **Authority** and the **generator**;

then, the **Authority** shall make a decision on the application as if this subpart, as it existed on 18 May 2023, continued in force.

"(2) Once the Authority has made a decision on an application to which subclause (1) applies, the matters and arrangements which were subject of the application shall be dealt with in accordance with this subpart.

"(3) Where:

"(a) an application has been made to the **Authority** for clearance of a **materially large contract** pursuant to clause 13.272 prior to 19 May 2023; and

"(b) the **Authority** has, pursuant to clause 13.273(1)(a), provided a clearance by notice in writing prior to 19 May 2023;

then, the **materially large contract** and the matters and arrangements which were subject of the application, shall be dealt with in accordance with this subpart.

Glossary of abbreviations and terms

Authority	Electricity Authority
Act	Electricity Industry Act 2010
ASX	Australian Securities Exchange Limited
Best alternative value	What the generator, acting rationally, could reasonably expect to earn over the duration of the contract, for the volume of electricity in the contract and other resources allocated to support the contract, in the absence of the contract and taking into account any credible threat to consumption
CFD	Contracts For Differences
Code	Electricity Industry Participation Code
Credible threat to consumption	Contracts which involve a 'credible threat to consumption' relate to a situation where a customer is likely to otherwise exit or not enter the market (i.e. not be attracted to locate domestically) or a customer who otherwise would reduce or not expand consumption
Distinctive value components	Distinctive value components are taken into account in the calculation of the value of the contract to the generator and the generator's best alternative where they are reasonably relevant. Distinctive value components may include but are not limited to: the contract price and any other relevant value features of the contract such as location, load profile, demand response and price separation provisions, clauses 'pegging' the electricity price to the trading conditions facing the large load user e.g. electricity price is linked to the price of aluminium, counterparty credit risk, value of maintaining an uninterrupted commercial relationship and any forms of financial support provided by the generator
Issues Paper	Inefficient Price Discrimination in the Wholesale Electricity Market – Issues and Options
MLC	Materially Large Contract - contracts (or combinations of contracts) relating to physical consumption of a quantity of electricity of net 150MW or more
Net 150 MW threshold	150 MW threshold less any MW consumed by the large load user from a new generation asset built a consequence of the contract
Net value of the MLC to the generator	The net value of the materially large contract to the generator is the value of the contract to the generator less the value of the generator's next best alternative.
NZAS	New Zealand Aluminium Smelter
OTC	Over The Counter Contract
PPA	Power Purchase Agreement

Rent seeking	A situation where an entity seeks to capture more wealth for themselves without adding to, and potentially destroying, wealth to society - by way of a sophisticated form of economic withholding. Generators effectively withhold supply to consumers by supplying electricity to a large load user that would otherwise have exited (or not entered the market) if they faced the true direct value of that electricity
Review Paper	Market Monitoring Review of Structure Conduct and Performance in the Wholesale Electricity Market - Information Paper
Tiwai contracts	Contracts between reservations made in the Review is that the price discrimination implicit in the 'Tiwai contracts' between Meridian Energy, Contact Energy and New Zealand Aluminium Smelters (NZAS)
UTS	Undesirable Trading Situation
Value of the contract to the generator	The value of the contract to the generator should take into account direct value components including the contract price and additional distinctive value components, both positive and negative.
Value of maintaining an uninterrupted commercial relationship	The value of the option to wait and during that period gain information which reduces the likelihood of making costly and irreversible decisions