

Electricity Industry Participation Code Amendment (Restrictions on Materially Large Contracts) 2022

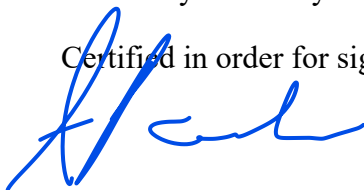
Under sections 38 and 40 of the Electricity Industry Act 2010, I make the following urgent amendment to the Electricity Industry Participation Code 2010.

At United Kingdom this 17th day of August 2022



Dr Nicola Lane Crauford
Chair
Electricity Authority

Certified in order for signature:



Alexandra Parker
Senior Legal Counsel
Electricity Authority



Jenny Stevens
Partner
Bell Gully

17 August 2022

17 August 2022

Contents

1	Title	1
2	Commencement and expiry	1
3	Code amended	2
4	Clause 1.1 amended (Interpretation)	2
5	Part 13, subpart 7 inserted	2

Amendment

1 Title

This is the Electricity Industry Participation Code Amendment (Restrictions on Materially Large Contracts) 2022.

2 Commencement and expiry

- (1) This amendment comes into force on the day after the amendment is published in the *Gazette*.
- (2) This amendment expires on the date that is 9 months after the date on which it comes into force.

3 Code amended

This amendment amends the Electricity Industry Participation Code 2010.

4 Clause 1.1 amended (Interpretation)

- (1) In clause 1.1(1), insert in its appropriate alphabetical order:
“**materially large contract**, for the purposes of subpart 7 of Part 13, has the meaning given to it by clause 13.268”.
- (2) In clause 1.1(1), definition of **buyer**,—
 - (a) after “**buyer**, for the purposes of subpart 5”, insert “and subpart 7”; and
 - (b) after “agrees to be the **buyer** for the purposes of subpart 5”, insert “or subpart 7 (as applicable)”; and
 - (c) after paragraph (c)(iii), insert:
“(d) for the purposes of subpart 7 of Part 13, in respect of any other contract, the **party** consuming the **electricity** that the contract relates to”.
- (3) In clause 1.1(1), definition of **contract for differences**, after “subpart 5”, insert “and subpart 7”.
- (4) In clause 1.1(1), definition of **party**,—
 - (a) after “subpart 5”, insert “and subpart 7”; and
 - (b) after “may be”, insert “, and for the purposes of subpart 7 of Part 13, means either the **buyer** or **seller** under a contract or both the **buyer** and **seller** under a contract, as the case may be”.
- (5) In clause 1.1(1), definition of **risk management contract**, after “subpart 5”, insert “and subpart 7”.
- (6) In clause 1.1(1), definition of **seller**,—
 - (a) after “**seller**, for the purposes of subpart 5”, insert “and subpart 7”; and
 - (b) after “agrees to be the **seller** for the purposes of subpart 5”, insert “or subpart 7 (as applicable)”; and
 - (c) after paragraph (c)(iii), insert:
“(d) for the purposes of subpart 7 of Part 13, in respect of any other contract, the **party** who is not the **buyer**”.

5 Part 13, subpart 7 inserted

After clause 13.266, insert:

“Restrictions on materially large contracts

“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) 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 that each satisfy paragraph (a)(i)–(ii) and when taken together satisfy paragraph (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** 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** 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).
- “(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** consumed from 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 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:
 - “(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-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-selling arrangements if the **generator** is relying on clause 13.269(1)(b) to give effect to the **materially large contract**.
- “(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 30 **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** 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, 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** re-selling arrangements and the **Authority** provided its clearance on the basis of clause 13.269(1)(b).
- “(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.”

Explanatory Note

This note is not part of the amendment, but is intended to indicate its general effect.

This amendment to the Electricity Industry Participation Code 2010 comes into force on the day after the amendment is published in the *Gazette* and expires on the date that is 9 months after the date on which it comes into force.

The amendment inserts a new subpart 7 of Part 13 into the Electricity Industry Participation Code 2010 (“Code”). The new subpart places certain restrictions on generators giving effect to materially large contracts entered into, extended or modified on or after the date the amendment comes into force. The amendment also provides for disclosure of materially large contracts and additional material, an ability for generators to seek Authority clearance of materially large contracts, and reconsideration and appeal of Authority clearance decisions.

The Authority published *Inefficient price discrimination in the wholesale electricity market – Issues and options* (Issues Paper) in October 2021 as an initial response to an observation made in its *Market Monitoring Review of Structure, Conduct and Performance in the Wholesale Electricity Market*. The primary intent of the Issues Paper was to explore whether generators have incentives under the current market design and regulation which can lead to arrangements which are inefficient and cause harm to consumers, using the Tiwai contracts to illustrate this potential. Having considered submissions in response to the Issues Paper, the Authority will shortly release a further consultation paper on the Authority’s website inviting submissions on a proposed permanent Code amendment that seeks to address generators’ incentives and ensure market participants are confident that any future arrangements are efficient and in the long-term interests of all consumers. The problem definition and rationale for the proposed permanent amendment as set out in detail in the further consultation paper also applies to this urgent amendment.

Pursuant to section 40 of the Electricity Industry Act 2010, the Authority considers that it is necessary or desirable in the public interest that the amendment be made urgently because:

- (i) The Authority has identified an issue with the current market design and regulatory settings whereby generators have incentives to enter into materially large contracts that are inefficient and are harmful to the long-term interests of consumers.
- (ii) There is a real risk of parties entering into such arrangements before any permanent regulatory solution can be fully consulted on and put in place,

including because parties may be motivated to avoid the signalled potential regulation.

- (iii) This has the potential to lock in inefficient price discrimination for many years causing inefficiencies in the electricity industry and material and ongoing harm to consumers.
-