

# Voluntary Code of Conduct

## For participants in New Zealand's Over the Counter Electricity Market

### Introduction

1. This Code of Conduct (**Code**) is the outcome of an Electricity Authority (the **Authority**) initiative, which commenced in December 2022, to facilitate the establishment of an OTC Electricity Market Working Group (**Working Group**).
2. The Authority's motivations for facilitating the establishment of the Working Group at that time included:
  - 2.1. The Authority's view that access to competitively priced risk management products is critical to confidence that electricity markets are ultimately serving the long-term interests of consumers – the Over the Counter (**OTC**) market's distinctive features, relative to formal exchanges, makes it best placed to provide flexible, bespoke, and less liquid risk management solutions.
  - 2.2. Disruptions to some market participants' access to exchange traded New Zealand electricity contracts at that time was increasing the reliance on the OTC market to execute their risk management strategies - putting added focus on the performance of the OTC market.
  - 2.3. The increasing importance of the OTC market to support the transition to clean energy, due to an increasing reliance on new investment and intermittent generation, which will increase demand for more bespoke risk management products – something the OTC market is uniquely placed to support.
3. Confidence in the overall design of New Zealand's electricity market will be increasingly dependent on the performance of the OTC market.
4. The Authority considered it appropriate to give an industry-led working group the opportunity to explore ways to improve the efficiency and performance of, and conduct within, the OTC market.
5. The OTC market:
  - 5.1. relies upon individuals' incentives to participate – there are no mandated participation requirements, rather the market relies on voluntary "point-in-time" participation
  - 5.2. utilises flexible bilateral contracting to enable greater customisation of risk management solutions than is typically afforded by products traded over more formal exchanges

- 5.3. has relatively low compliance and transactional costs which is a key feature to encourage participation.
6. For these reasons the Authority considered that OTC participants are, in the first instance, best placed to develop a view on how the OTC market should perform for the ultimate long-term benefit of consumers in our electricity markets and what, if anything, might be done voluntarily by industry to improve the OTC market's efficiency and performance and set efficient trading standards amongst participants.
7. The Working Group members represented a diverse range of industry interests, comprising representatives from 2degrees, Contact Energy, Genesis Energy, Manawa Energy, Mercury, Meridian Energy, Prime Energy, and The Energy Collective.
8. For the avoidance of doubt, while the Authority has facilitated the formation of the Working Group, the Working Group is not run or led by the Authority. The Authority's role was limited to the appointment of the initial Working Group members and resourcing the facilitation role for the Working Group.

#### **Why have a Code of Conduct**

9. Access to competitive risk management products, on competitive terms and conditions, is a foundation of an efficient electricity market which ultimately serves the long-term interests of consumers. Exchange traded and OTC markets each have distinctive but complementary roles to play in supporting risk management in a competitive and efficient electricity market.
10. This Code reflects the Working Group's consensus on the behaviours and conduct consistent with an efficient and competitive OTC market. The Code provides guidelines for behaviours which support improved performance of the OTC market and which will ultimately translate into outcomes that are in the long-term interests of consumers.

#### **Who does the Code Apply to?**

11. The Code is voluntary.
12. However, all participants in the OTC market are encouraged to sign up to the Code. The more participants that are signatories to the Code, the greater the confidence that behaviours in the OTC market will meet the efficient trading standards set out in the Code, and thereby enhance the efficiency of, and reduce the costs of doing business in, the OTC market.
13. By becoming a signatory to the Code the party is communicating their intention to comply with the Code in all their dealings in the OTC market.

14. Nothing in the Code restricts participation in the OTC market by any party. Parties wanting to participate in the market, but not sign the Code, are free to access and participate in the market as they always have, and signatories to the Code are free to transact with parties that are not signatories to the Code.

### **Status of the Code**

15. For the avoidance of doubt, this Code is neither binding on signatories nor does it have the force of law.

16. Rather the Code is a reflection of the principles and behaviours the signatories commit to in conducting their business, which they each consider support an efficient and competitive OTC market and, therefore, are ultimately consistent with advancing the long-term interests of New Zealand electricity consumers. Signatories commit to complying with the spirit of these principles and conducting their OTC business consistent with the Code. Each signatory recognises that its compliance with this Code, in part, serves as an indicator of the integrity of its conduct in the OTC market.

17. This Code serves as the foundation that signatories commit to complying with when participating in the OTC market. The Code is not a substitute for internal policies and procedures, which would typically provide added detail, and are tailored to reflect the specific nature of the signatory's OTC activities and desired culture more closely. Signatories commit to having internal cultures that encourage conduct and behaviours consistent with being an efficient and high integrity participant in the OTC market.

18. This Code in no way supersedes or alters the legal obligations of parties in the OTC market including compliance with the:

- 18.1. Commerce Act 1986 (**Commerce Act**)
- 18.2. Fair Trading Act 1986
- 18.3. Financial Markets Conduct Act 2013
- 18.4. Anti-Money Laundering and Countering Financing of Terrorism Act 200 and
- 18.5. Electricity Industry Act 2010 and Electricity Industry Participation Code

### **Consequences of non-compliance**

19. As this Code is neither binding on signatories nor does it have the force of law, there are no immediate or direct consequences from non-compliance with the Code.

20. Signatories recognise that the Authority may have an interest in monitoring participants' uptake and compliance with this Code, given the Code is intended to facilitate trading conduct that is consistent with an efficient and competitive wholesale market.

# The Code

## Underlying Principles

21. Signatories commit to the following principles in supporting an efficient OTC market that ultimately serves the long-term interests of New Zealand electricity market consumers.
  - 21.1 Competition and the long-term interests of electricity consumers are advanced by an efficient OTC market, which provides risk management products on terms and conditions that could be expected in a workably competitive wholesale market.
  - 21.2 Individual participants in the OTC market should support improved liquidity by facilitating entry and participation by other businesses that have the necessary capability and capacity (including financial capacity) to transact in the OTC market.
  - 21.3 All parties (subject to laws and regulations) have the right to determine at any point in time the risk management features of the trades they want to transact, the requirements they have on counterparties to complete these trades, and the terms and conditions they are willing to accept.
  - 21.4 Request for Proposals (RFPs) in the OTC market may not get transacted for a number of reasons, including parties having different opinions on the value of a trade, or because one party considers the other party is unable to satisfy their credit or capability requirements.
  - 21.5 It is in the interests of all parties to have the necessary assurances that trades are being transacted that would be commercially viable and provide value to both parties (as facilitating such trading will ultimately be in the long-term interests of consumers).
  - 21.6 The confidence in and efficiency of the OTC market is improved through encouraging high integrity conduct from all counterparties - which includes counterparties acting fairly, consistently and in good faith, and enabling their staff with the requisite skills, training, and support to perform their roles efficiently, effectively and professionally.
  - 21.7 RFP issuance and response practices should be adopted which are efficient so as to be mindful of the servicing costs and mitigate unnecessary uncertainty (for example by providing reasonable timelines, providing reasonably required information and being issued where there is a genuine intention to transact).
  - 21.8 There is a commitment to adopting trading practices and processes that are transparent, efficient, and objectively justifiable, and to there being ongoing improvement and monitoring of performance, both of the market as a whole and the individual participants, so as to ensure ongoing confidence in and efficiency of the OTC market.

## **All (prospective) participants are treated consistently**

22. Participants commit to the principle of treating all OTC market participants consistently and without prejudice.
23. Consistency does not mean that all participants will, for example, get the same response or the same terms and conditions.
24. Consistency means treating all parties fairly and in objectively justifiable ways, and in good faith without prejudice. More specifically, that the same methods and rules are applied to all parties seeking to participate in OTC transactions.
25. This includes the consistent application of the methods and rules in:
  - 25.1 Applying credit assessment processes and the making of credit approval decisions and setting associated credit limits
  - 25.2 Communication, efforts and responsiveness in servicing a request
  - 25.3 Determining whether or not to respond to an RFP with a proposal and price
  - 25.4 The terms and conditions of transactions.

## **Ability to transact in OTC markets and Onboarding prospective counterparties**

26. To facilitate onboarding of prospective counterparties and enhance all counterparties' capacity to transact in the OTC market, participants:
  - 26.1 Commit to an open and transparent credit assessment and review processes when assessing whether to undertake OTC trades with a specific counterparty, which among other things, includes:
    - 26.1.1 Communication:
      - 26.1.1.1 A willingness to discuss with the counterparty the general approach, key considerations and process for informing credit decisions, credit limits, and trading decisions, while recognising there are limits to what information should appropriately be shared, including in light of Commerce Act compliance obligations. For example, elements of the credit methodology and business strategy may be commercially sensitive and, therefore, not appropriate to share.

26.1.1.2 Upon request, sharing with the counterparty their credit status, and other information relevant to that counterparty in relation to limits and available capacity (again recognising that there may be limits to what information should appropriately be shared, including in light of Commerce Act compliance obligations).

26.1.2 Timeliness – Processing credit applications and reviews will be undertaken in a timely, efficient, and transparent manner, recognising unforeseen events may delay the process:

26.1.2.1 This includes providing an indication of when a decision might reasonably be made, subject to the applicant satisfying all reasonable information requirements in a timely manner.

26.1.2.2 Proactively notifying the applicant of any progress, including delays, issues or final decisions, when they become known.

27. Where a participant is wanting to establish or maintain trading relationships with a counterparty, the participant will provide the counterparty with the information the counterparty requests for the purposes of assessing credit worthiness and risk management capability in a timely and accurate manner, as long as the information requested is reasonable and relevant (and noting, as above, there are Commerce Act limits on what information can be shared).

28. Where a participant can reasonably anticipate trading with a counterparty in future, the participant will seek to have the requisite approvals and trading arrangements in place with that counterparty in advance of a specific proposal, so that the participant can transact any future business with the counterpart in a timely, efficient, and more certain manner.

29. Participants commit to investigating the extent to which the development of industry standard credit documentation (including default ISDA schedules) may in future be an efficient starting point for conversations with any prospective counterparty:

29.1. recognising that this does not imply an obligation to agree to use the standard documentation in any specific case; and

29.2. rather it would be a starting point for negotiations, and variations may be expected in each specific case.

### **Efficient operation of the OTC market**

30. To reduce the costs of participating and transacting in the market, and enhance efficiency, certainty and understanding among participants, participants will endeavour to:

- 30.1. only issue RFPs when the issuer has a genuine intent to transact.
- 30.2. ensure RFPs issued include reasonable timeframes for providing responses.
- 30.3. when contemplating issuing a relatively novel and/or complex RFP (with relatively high costs for prospective respondents to evaluate before submitting a proposal), the issuer will consider a two-stage procurement:
  - 30.3.1. Expression of Interest stage (**EOI stage**) – with the goal of seeking high level feedback on the proposed structure of the transaction, whether it could be made more attractive to offer on, and prospective responders’ appetite for this type of transaction. This information would inform the shape and targeting of any future RFP by the issuer.
  - 30.3.2. RFP stage – this stage would only be required if there is evidence of sufficient interest following the EOI stage.
- 30.4. Having determined to reject a response to an RFP, the issuer will notify the respondent of the rejection as soon as practical, including the reason for the rejection.
- 30.5. All parties that receive RFPs should endeavour to respond with a price whenever possible as increased participation will result in increased competitiveness of the OTC market. Where a party does not intend to respond with a price they should advise the RFP issuer in a timely way and provide a reasonable explanation of the reasons (noting there are limits on what information can be disclosed).
  - 30.5.1. Electricity market participants with significant wholesale market share should resource their business to limit the number of instances when they are not in a position to respond with a priced proposal. These instances being limited to occasions where the RFP issuer’s credit standing does not accommodate the requested deal structure, the RFP responder is not well placed to respond competitively on the RFP because the structure results in an intolerable risk position, or constrained resourcing doesn’t allow a response within the requested timeframe. In all instances, as much explanation as is reasonable to provide should be provided.
- 30.6. Where a participant considers it could be helpful to facilitate efficient trading with a counterparty (either as part of a current proposal, or to facilitate future trading when rejecting a current proposal), and subject to considering issues of commercial sensitivity and Commerce Act compliance, the participant may elect to provide the counterparty with details of the factors relevant to it in considering trading proposals.
- 30.7. Where a participant anticipates credit constraints arising with respect to a counterparty’s specific response to a RFP, it may consider suggesting changes to

the structure of the proposed transaction or the use of credit support (eg guarantees, letters of credit and other collateral) which could increase its appetite to transact with the counterparty and/or improve the pricing in its proposal.

### **Performance and monitoring**

31. The Working Group supports regular monitoring of the OTC market by the Authority to ensure the market as a whole and the individual participants in it are performing in a manner which is efficient and competitive (and, therefore, ultimately in the long-term interests of consumers).



**SIGNED ON BEHALF OF [COMPANY NAME]**

**Name**

**Job title**

**Signature**

**Date**