



ISSN NO. 0114-2720
J6315

COMMERCE COMMISSION

Decision No. 517

Determination pursuant to the Electricity Industry Reform Act 1998 (the EIR Act), in the matter of an application for exemption of an involvement and an interests in an electricity lines business and an electricity supply business from the application of the EIR Act. The application is made by:

Dr Keith Turner

The Commission:	Paula Rebstock Peter JM Taylor
Summary of the Application	Dr Keith Turner is involved in both Meridian Energy Ltd (Meridian), an electricity supply business, and Auckland International Airport Ltd AIAL), an electricity lines business. He seeks exemption from the application of section 17 of the EIR Act, in order to become involved in both kinds of business.
Determination:	The Commission, in terms of section 81 of the EIR Act, exempts Dr Turner from the application of section 17 of the EIR Act in relation to a prohibited cross-involvement in an electricity lines business and an electricity supply business. The exemption is subject to the conditions stated in this Decision.
Date of Determination:	17 March 2004
Date of Exemption:	The exemption takes effect from the date of the publication of a Notice of Exemption in the <i>New Zealand Gazette</i> .

CONTENTS

INTRODUCTION	1
DECISION 384	1
MERIDIAN ENERGY AS AN ELECTRICITY SUPPLY BUSINESS	1
AIAL AS AN ELECTRICITY LINES BUSINESS	2
DR TURNER'S INVOLVEMENTS IN MERIDIAN AND AIAL	2
PROHIBITED CROSS-INVOLVEMENT	3
COMMISSION PROCEDURES	3
General	3
Criteria Used by the Commission to Consider Exemption Applications	3
RELEVANT MARKETS	4
DR TURNER'S SUBMISSIONS IN SUPPORT OF HIS APPLICATION FOR EXEMPTION	4
EXAMINATION OF DR TURNER'S INVOLVEMENTS IN TERMS OF THE COMMISSION'S CRITERIA	5
Incentives or Opportunities of Dr Turner to Inhibit Competition in the Electricity Industry	5
Incentives or Opportunities of AIAL to Cross-subsidise Meridian's Generation Activities From its Line Business Resulting from Dr Turner's Presence as Chief Executive of Meridian and a Director of AIAL	6
A Relationship between Meridian and AIAL Not at Arms Length due to Dr Turner's Presence as Chief Executive of Meridian and a Director of AIAL.	6
THE COMMISSION'S DECISION	6
NOTICE OF EXEMPTION	8

INTRODUCTION

- 1 On 10 February 2004, AIAL applied to the Commerce Commission (the Commission) for exemption from the application of section 17 of the EIR Act in respect of its intention to appoint Dr Keith Turner, Chief Executive of Meridian to its Board of Directors.
- 2 As such an appointment would not cause AIAL to have material influence over Meridian and would not therefore cause AIAL to become cross-involved in an electricity lines business and an electricity supply business, the Application was varied by consent so that Dr Turner, who would be cross-involved, is the Applicant.
- 3 Dr Turner's involvements in electricity businesses arise from his being Chief Executive of Meridian, and his potential appointment to the Board of AIAL.
- 4 The Commission's powers to exempt businesses, involvements or interests from the application of the EIR Act or persons from compliance with any provisions of any regulations made under the EIR Act are specified in section 81 of the EIR Act.

DECISION 384

- 5 In March 2000, the Commission granted Ms Joan Withers an exemption from section 17 of the EIR in respect of cross-involvement through her directorships of the AIAL Board and the Meridian Board. The written reasons for that exemption are contained in the Commission's Decision 384.
- 6 Miss Withers remains on the boards of Meridian and AIAL. The Commission considers that the circumstances of Dr Turner's application for exemption are almost identical to those presented to it in respect of Ms Withers.

MERIDIAN ENERGY AS AN ELECTRICITY SUPPLY BUSINESS

- 7 Meridian is an electricity generator and retailer. It was formed as a result of the division of Electricity Corporation of New Zealand into three separate companies in April 1999 and is a State Owned Enterprise.
- 8 It owns Manapouri Power Station, eight power stations on the Waitaki River and the Wellington wind powered generator. The total capacity of its power stations is around 2500 megawatts.
- 9 In addition, Meridian is the incumbent electricity retailer selling electricity over the networks of Northpower Ltd, ScanPower Ltd, Centralines Ltd and Network Waitaki Ltd and also is retailing to electricity customers in other locations throughout New Zealand.
- 10 In terms of the EIR Act, Meridian:
 - sells electricity in New Zealand (s5(1)(a)(i));
 - generates electricity in New Zealand (s5(1)(a)(iii));
 - owns and operates directly generators in New Zealand (s5(1)(b));

- owns and operates directly core assets of an electricity retail business which include the benefit of contracts to sell electricity (s5(1)(c)); and
- does not fall within any of the exclusions listed in section 5(2) or 5(3).

11 Therefore, Meridian is an electricity supply business in terms of the EIR Act.

AIAL AS AN ELECTRICITY LINES BUSINESS

12 AIAL is a public company listed on the New Zealand Stock Exchange. It owns and operates the Auckland Airport. Its major shareholders are the New Zealand Central Securities Depository Limited, Citicorp Nominees Pty Limited, and the Auckland and Manukau City Councils.

13 AIAL owns an electricity distribution network at the Airport. The network operates at 11,000 and 400 volts and comprises transformers, switchgear and underground cables. The network connects to Vector Ltd's citywide network at the perimeter of the Airport. AIAL is a lines customer of Vector Limited.

14 AIAL distributes electricity to 220 consumers at the airport¹. AIAL levies a line charge on the consumers for the provision of such line function services².

15 In terms of the EIR Act, AIAL:

- conveys electricity by line in New Zealand (s4(1)(a));
- owns and operates, directly, lines in New Zealand and other core assets of an electricity lines business (s4(1)(b)); and
- does not fall within any of the exclusions listed in section 4(2).

16 Therefore, AIAL is an electricity lines business in terms of the EIR Act.

DR TURNER'S INVOLVEMENTS IN MERIDIAN AND AIAL

17 Dr Turner is the chief executive of an electricity supply business and wishes to be a director of an electricity lines business. In terms of the EIR Act:

- Meridian and AIAL are both body corporates and Dr Turner is a "manager" of both (s3);
- without limiting the ordinary meaning of the expression "material influence", a manager of a person that carries on an electricity business is deemed to have material influence over the electricity business (section 11(1)(a)); and
- a person is involved in an electricity business if the person has material influence over the business (section 7(1)(c))

¹ Of the 80 gigawatt-hours per annum distributed, 23 is for AIAL's own use.

² Electricity retailers TrustPower Ltd, Genesis Power Ltd, Contact Energy Ltd, and Mighty River Power Ltd each have access to AIAL's network in order that they may retail electricity to consumers connected to AIAL's network.

- 18 Therefore, on his appointment to the AIAL, Dr Turner, as a result of his management position with Meridian and his directorship of AIAL, would be involved in both an electricity supply and an electricity lines business.

PROHIBITED CROSS-INVOLVEMENT

- 19 Section 17 of the EIR Act provides:

- (1) No person involved in an electricity lines business may be involved in an electricity supply business.
- (2) No person involved in an electricity supply business may be involved in an electricity lines business.

- 20 Dr Turner's appointment to the board of AIAL would mean that he is involved, and wished to remain involved, in both an electricity lines and an electricity supply business. He would have, in terms of section 17 of the EIR Act, a prohibited cross-involvement.

- 21 Dr Turner has, therefore, applied to the Commission for exemption from the application of section 17 of the EIR Act.

COMMISSION PROCEDURES

General

- 22 For the purpose of considering this application for exemption, the Commission, in terms of section 58 of the EIR Act which applies section 105 of the Commerce Act 1986 to the EIR Act, has delegated its powers under section 81 of the EIR Act to PR Rebstock and PJM Taylor.

- 23 The Commission's decision is based on an investigation conducted by its staff and their subsequent advice to the Commission.

Criteria Used by the Commission to Consider Exemption Applications

- 24 The EIR Act gives the Commission wide powers of enforcement, extension and exemption. To provide assistance to parties affected by the EIR Act, the Commission set out its role and processes in Practice Note No.3.³

- 25 The Commission stated in Practice Note No.3 that:

"The EIR Act provides for the Commission to make exemptions in terms of section 81 of the Act. In considering applications for exemptions, the Commission will have specific regard to the particular purpose of Parts 1 to 5 of the EIR Act as defined in section 2(2) of the EIR Act. The Commission is likely to grant an exemption in respect of a business or involvement or interest only wise doing so:

- (a) would not result in certain involvements in electricity lines businesses and electricity supply businesses which may create incentives or opportunities:
 - (i) to inhibit competition in the electricity industry; or
 - (ii) to cross-subsidise generation activities from electricity lines businesses; and
- (b) would not result in relationships between electricity lines businesses and electricity supply businesses which are not at arms length.

³ Practice Note No.3, September 1998, Electricity Industry Reform Act 1998 Commission's Role and Processes.

In determining exemptions, the Commission will also have regard to the overall purpose of the EIR Act as set out in section 2(1) of the Act. That is, the purpose of the EIR Act is to reform the electricity industry to better ensure that:

- (a) costs and prices in the electricity industry are subject to sustained downward pressure; and
- (b) the benefits of efficient electricity pricing flow through to all classes of consumers by –
- (c) effectively separating electricity distribution from generation and retail; and
- (d) promoting effective competition in electricity generation and retail.”

26 The Commission noted in Practice Note No.3 that:

“...the EIR Act provides for maximum cross-ownership limits and specific structural and behavioural requirements to ensure that the purposes of the Act are met. Strict compliance with these limits and requirements is, other than in exceptional circumstances,⁽⁴⁾ expected.”

27 The Commission stated in Practice Note No.3 that:

“On receipt of an application in the proscribed form, the Commission will determine whether granting an exemption would be contrary to any element of the particular purpose of Parts 1 to 5 of the EIR Act or the overall purpose of the Act.

The Commission’s tests would necessitate obtaining and evaluating objective answers to the following three questions in relation to the particular purpose of Parts 1 to 5 of the EIR Act:

- Would the Commission, by granting an exemption in respect of a business or involvement or interest, create incentives or opportunities to inhibit competition in the electricity industry?
- Would the Commission, by granting an exemption in respect of a business or involvement or interest, create incentives or opportunities to cross-subsidise generation activities from electricity lines businesses?
- Would the Commission permit, by granting an exemption in respect of a business or involvement or interest, a relationship between an electricity lines business and an electricity supply business which is not at arms length?

In relation to these questions, the Commission will consider factors such as:

- Relevant market(s)⁵ within the electricity industry;
- The nature of any incentives or opportunities created;
- The temporal nature of any incentives or opportunities created;
- The nature of any relationship which is not at arms length; and
- The temporal nature of any relationship which is not at arms length.”

RELEVANT MARKETS

28 Electricity generation and electricity retail markets in New Zealand, and AIAL’s local electricity distribution market are relevant to the application of the Commission’s criteria to the facts of Dr Turner’s application for exemption.

DR TURNER’S SUBMISSIONS IN SUPPORT OF HIS APPLICATION FOR EXEMPTION

29 Dr Turner submitted that his involvement in AIAL and Meridian will not create incentives or opportunities which will inhibit competition in the electricity industry or cross-subsidise generation activities from electricity lines businesses, and will not result

⁴ For example, of the types provided for in section 19 of the EIR Act.

⁵ Defined using the same process as used for market definitions in respect of Commerce Act matters.

in relationships between an electricity lines business and an electricity supply business which are not at arms length, on the grounds that follow.

- (a) As with Ms Withers' application "there is no mechanism whereby [Dr Turner's] cross-involvements could provide incentives or opportunities in electricity markets", and the possibility of Meridian supplying consumers connected to AIAL's network in the future does not arise. This is because a condition of the exemption granted to Ms Withers is that AIAL and Meridian shall not contract for the supply of electricity while Ms Withers is on both boards.
- (b) The fact that the two businesses are not at arms length will continue to be tempered by the fact that there is an absence of connection or relationship between the companies and practically no method of creating one in the future.
- (c) Dr Turner's influence is no more material than that of Ms Withers' and in any case, the AIAL constitution would prohibit Dr Turner from voting on any matter relating to a transaction in which they have an interest.

EXAMINATION OF DR TURNER'S INVOLVEMENTS IN TERMS OF THE COMMISSION'S CRITERIA

Incentives or Opportunities of Dr Turner to Inhibit Competition in the Electricity Industry

- 30 The focus of this enquiry is on the only market which the two companies have in common. That is, on the retail electricity market comprising the 220 consumers connected to AIAL's distribution network at Auckland Airport, and whether an exemption would provide either Meridian or AIAL with incentives or opportunities to inhibit competition in that market.
- 31 In the absence of any existing or future connection or relationship between Meridian and AIAL, other than that due to the presence of Dr Turner's position as Chief Executive of Meridian and his presence on AIAL's Board, the Commission considers that there is no mechanism presently whereby Dr Turner's cross-involvements could provide incentives or opportunities to inhibit competition in electricity markets.
- 32 However, should Meridian in future supply electricity to consumers connected to AIAL's network, the Commission considers there would exist the opportunity for competition to be affected. While the Commission accepts that Dr Turner could not vote on matters on which he had declared a conflict of interest, it considers that there would be the opportunity for competition to be inhibited by means other than by the formal voting process.
- 33 The Commission considers that Dr Turner cannot rely on the conditions attached to Ms Withers' exemption to act as a mechanism preventing AIAL from gaining an incentive or opportunity to inhibit competition in electricity markets. The Commission notes that the conditions of Ms Withers' exemption apply only as long as her cross-involvements and that Dr Turner's cross-involvements may extend beyond this.

Incentives or Opportunities of AIAL to Cross-subsidise Meridian's Generation Activities From its Line Business Resulting from Dr Turner's Presence as Chief Executive of Meridian and a Director of AIAL

- 34 In spite of the Applicant's statement to the contrary, the Commission does consider this criteria to be relevant.
- 35 Presently there is no connection or relationship between the two companies which would afford cross-subsidisation. However, the Commission considers there exists the potential mechanism, by which AIAL's electricity lines business could be used to subsidise Meridian's generation activities. This could occur via a use-of-system agreement negotiated between Meridian and AIAL, which did not provide a commercial return to AIAL, and that the opportunity for the negotiation of such an agreement could be influenced by the presence of Dr Turner as a person having material influence in the two companies.
- 36 However, while Dr Turner is cross-involved, providing no relationship or connection can be formed between the two companies which would afford the ability to cross-subsidise, the Commission considers that AIAL would have no incentives or opportunities to cross-subsidise Meridian's generation activities from its lines businesses.

A Relationship between Meridian and AIAL Not at Arms Length due to Dr Turner's Presence as Chief Executive of Meridian and a Director of AIAL.

- 37 Dr Turner proposes to become a director of AIAL's electricity lines business and continue as Chief Executive of Meridian's electricity supply business. The two businesses will have, in common, a person deemed to have material influence on each. On the face of it, the relationship between Meridian's electricity supply business and AIAL's electricity lines businesses will not be at arms length.
- 38 However, the Commission considers that the potential effects of the relationship not being at arms length can be tempered by the fact that there is no connection or relationship between the two companies and practically no method by which the non-arms length relationship could be used to promote the mischief which the EIR Act seeks to prevent. As a result, under these conditions, the Commission does not consider the potential effects of the relationship not being at arms length would be likely to suborn the purposes of the EIR Act.

THE COMMISSION'S DECISION

- 39 The Commission considers that provided there is no relationship between the two companies in which Dr Turner would be cross-involved, his application passes the Commission's criteria for granting exemptions from section 17 of the EIR Act. Therefore, the Commission has decided to exempt Dr Turner from the application of section 17 of the EIR Act subject to certain conditions.
- 40 In making its decision the Commission has taken into account the fact specific circumstances revealed in Dr Turner's application for exemption. Those facts are essentially the absence of any connection or relationship between the electricity supply and electricity line businesses of which Dr Turner is involved. The Commission has

made it a condition of the exemption that there should not in future be any connection or relationship between the two companies in respect of electricity supply or distribution whilst Dr Turner remains involved in both. By this the Commission means that Meridian should not become an electricity retailer to consumers connected to AIAL's electricity distribution network.

- 41 The Commission notes that section 81(5) provides that the Commission may vary or revoke any exemption at any time.
- 42 Therefore, having considered the stated criteria, the Commission exempts Dr Turner from the application of section 17 of the EIR Act, subject to the terms and conditions specified in the Notice of Exemption.

NOTICE OF EXEMPTION

The Commission, pursuant to section 81, exempts Dr Keith Turner from the application of section 17 of the Electricity Industry Reform Act 1998 in relation to a prohibited cross-involvement in an electricity lines and an electricity supply business.

The exemption is subject to the following terms and conditions:

- (a) That, Meridian Energy Ltd shall not enter into any kind of contract or arrangement with Auckland International Airport Ltd that relates to the use of Auckland International Airport Ltd's electricity distribution network whilst Dr Turner is involved with Meridian Energy Limited and a director of Auckland International Airport Ltd; and
- (b) That Dr Turner informs the Commission if he becomes a director of any company other than those described in his application for exemption.

The Commission may vary or revoke this exemption in accordance with section 81(5) of the EIR Act.

The exemption takes effect from the date of publication of this Notice in the *Gazette*.

Dated this 17th day of March 2004

Paula Rebstock
Chair