



COMMERCE COMMISSION

Decision No. 682

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

MARK TUME

The Commission:

M N Berry
P J M Taylor

Summary of Application:

Application by Mark Tume for exemption from the application of the EIR Act in respect of certain prohibited involvements in Powerco Limited's lines and in the generation and sale of electricity by TrustPower Limited.

Determination:

The Commission, pursuant to section 81 of the EIR Act, determines to grant an exemption from compliance with section 17(2)(a) of the EIR Act, but with the conditions specified in the Notice of Exemption.

Date of Determination:

10 November 2009

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SQUARE BRACKETS**

CONTENTS

INTRODUCTION	3
COMMISSION PROCEDURES	3
General	3
Criteria Used by the Commission to Consider Exemption Applications	3
PARTIES	5
Mr Tume	5
Other Parties.....	5
MARK TUME’S APPLICATION	7
APPLICATION OF THE EIR ACT TO MR TUME	7
Involvements.....	7
Mr Tume’s Potential Prohibited Involvements	9
MR TUME’S SUBMISSIONS IN SUPPORT OF HIS APPLICATION	10
EXAMINATION IN TERMS OF THE COMMISSION’S CRITERIA	12
Relevant Markets	12
Question 1: Incentives or Opportunities to Inhibit Competition in the Electricity Industry	12
Question 2: Incentives or Opportunities to Cross-subsidise Generation or Retail Activities	13
Question 3: Requirement for Corporate Separation and Compliance with arm’s-length and use-of-system rules	14
Conclusion in Respect of the Commission’s Criteria	15
THE COMMISSION’S DETERMINATION.....	16
APPENDIX 1: TrustPower’s Generation Connected to Powerco’s Network	17
NOTICE OF EXEMPTION	18

INTRODUCTION

1. On 9 June 2009, the Commerce Commission (the Commission) registered an application (the Application) from Mark Tume (Mr Tume) for exemption from the application of the Electricity Industry Reform Act 1998 (the EIR Act).
2. Mr Tume's potential involvements in electricity businesses arise from his proposed appointment as a director of Powerco Limited (Powerco) an electricity lines business and his existing directorship of Infratil Limited (Infratil), a majority shareholder in TrustPower Limited (TrustPower) an electricity generation and sales business.
3. Mr Tume applied, under section 81 of the EIR Act, for exemption from the requirement to comply with the EIR Act in respect of these potential prohibited involvements.

COMMISSION PROCEDURES

General

4. For the purposes of considering this application for exemption, the Commission, in terms of section 73 of the Crown Entities Act 2004, has delegated its powers under section 81 of the EIR Act to M N Berry and P J M Taylor, Commission members.

Criteria Used by the Commission to Consider Exemption Applications

5. The EIR Act was amended in October 2008 by the Electricity Industry Reform Amendment Act 2008.
6. The EIR Act provides for the Commission to make exemptions in terms of section 81 of the EIR Act. In considering applications for exemptions, the Commission will have specific regard to the particular purpose of Parts 1 to 3 and 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 where doing so:
 - (a) would not result in certain involvements in electricity lines and electricity generation and retail that may create incentives or opportunities:
 - (i) to inhibit competition in the electricity industry; or
 - (ii) to cross-subsidise generation or retail activities from electricity lines activities; and
 - (b) where applicable, would not result in relationships between a business that has involvement in electricity lines and a business that has involvement in electricity generation or retail, where those relationships may not otherwise be at arm's length.
7. In determining exemption applications, 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:
 - (a) that costs and prices in the electricity industry are subject to sustained downward pressure; and

- (b) that the benefits of efficient electricity pricing flow through to all classes of consumers; and
 - (c) new investment in generation from renewable energy sources
- by –
- (d) effectively separating electricity lines from generation and retail where those activities are co-located; and
 - (e) promoting effective competition in electricity generation and retail; and
 - (f) limiting barriers to new investment in generation from renewable energy sources.
8. On receipt of an application in the prescribed form, the Commission will determine whether granting an exemption would be contrary to any element of the particular purpose of Parts 1 to 3 and 5 of the EIR Act or the overall purpose of the EIR Act.
9. The Commission's test necessitates obtaining and evaluating objective answers to the following questions in relation to the particular purpose of Parts 1 to 3 and 5 of the EIR Act:
- 1. 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?
 - 2. Would the Commission, by granting an exemption in respect of a business or involvement or interest, create incentives or opportunities to cross-subsidise generation or retail activities from electricity lines activities?
 - 3. Where applicable, would the Commission permit, by granting an exemption in respect of a business or involvement or interest, a relationship between a business that has involvement in electricity lines and a business that has involvement in electricity generation and retail, where those relationships may not otherwise be at arm's length?
10. In relation to these questions, the Commission will consider such factors as:
- 1. The relevant market(s)¹ within the electricity industry;
 - 2. The nature of any incentives or opportunities created;
 - 3. The temporal nature of any incentives or opportunities created;
 - 4. The nature of any relationship that is not at arm's length; and
 - 5. The temporal nature of any relationship that is not at arm's length.
11. In the particular circumstances of this case, the Commission decided to invite submissions on the Application. The Commission received one submission on this Application, from Genesis Energy Limited. The submission was not in support of a conditional exemption, as proposed in the Application, being granted to Mr Tume.

¹ Defined using the same market definition process as applied in Commerce Act matters. See also Commerce Commission, *Mergers and Acquisitions Guidelines*, 1 January 2004.

12. Genesis considers that the conditions proposed by Mr Tume are narrow compared with the conditions the Commission applied in Decision 629² relating to Lloyd Morrison's directorship of Auckland International Airport Limited. Genesis is particularly concerned the proposed conditions target the potential for discussions and decisions to advantage TrustPower, but do not address any potential for disadvantaging TrustPower's competitors. Genesis also maintains the proposed conditions fail to address the risk of privileged disclosure of the outcomes of discussions and decisions.
13. Genesis considers, from a pro-competitive point of view, any exemption granted to Mr Tume should not have conditions any lesser than the conditions applying to Mr Morrison's exemption with respect to Auckland International Airport Limited. However, given that electricity distribution is a core business activity for Powerco, Genesis also does not consider it credible that Mr Tume could act as a director of Powerco under those conditions. As such, Genesis does not consider it credible that granting Mr Tume an exemption could be considered consistent with the purpose of the EIR Act.
14. Other than the matters discussed below in paragraphs 67 to 72, the Commission agrees that any exemption granted to Mr Tume should not have conditions any the lesser than the conditions applying to Mr Morrison's exemption with respect to Auckland International Airport Limited. However, as is discussed below, Mr Tume's potential prohibited involvement arises from the generation cap rule that did not apply to Mr Morrison. Hence, while any conditions applying to the exemption that the Commission grants to Mr Tume (as explained later) will not be any the lesser, but they will be different.

PARTIES

Mr Tume

15. Mr Tume is currently a director of Infratil which owns a 50.5% shareholding in TrustPower. Powerco wishes to appoint Mr Tume to its Board of Directors.

Other Parties

Infratil

16. Infratil is a specialist investor in infrastructure and utility assets and is listed on the New Zealand Stock Exchange. One of Infratil's investments is a 50.5% shareholding in TrustPower, an electricity generator and retailer.

TrustPower

17. TrustPower is New Zealand's fourth largest electricity retailer, selling electricity throughout New Zealand. TrustPower's generation assets that are connected to Powerco's network are:
 - (a) hydro stations at Kaimai in the Bay of Plenty – a scheme of four stations with a total nameplate capacity of 41.9 MW and an annual output of [] GWh. The Kaimai scheme consists of the Kaimai 5 Station (0.3 MW) commissioned in 1994, the Lloyd Mandeno Station (16 MW) commissioned in 1972, the Lower Mangapapa Station (5.6 MW) commissioned in 1979, and the Ruahihi Station (20 MW) commissioned in 1983;

² Commerce Commission, *Decision 629: Lloyd Morrison*, 19 November 2007.

- (b) a hydro station at Patea in South Taranaki – commissioned in 1983/84, the Patea Hydro Station has a nameplate capacity of 31.4 MW and an annual output of [] GWh;
 - (c) the Mangorei Power Station in Taranaki – commissioned in 1931, nameplate capacity of 4.5 MW and annual output of [] GWh;
 - (d) the Motukawa scheme – commissioned in 1927, nameplate capacity of 4.6 MW and annual output of [] GWh; and
 - (e) the Tararua wind farm above Palmerston North – stage one of the wind farm (34 MW) was commissioned in 1999 and has an annual output of [] GWh, and stage two (34 MW) was commissioned in 2004 and has an annual output of [] GWh.
18. TrustPower sells electricity to approximately [] customers on Powerco’s network ([]% of all Powerco’s connected customers). For the 12 months to 30 June 2009, TrustPower sold [] GWh to these customers ([]% of the total energy conveyed by Powerco).
 19. TrustPower has two major shareholders. Infratil is the largest with a 50.5% shareholding and TECT³ Holdings Limited has a 32.9% shareholding. There are nearly 13,000 other shareholders in TrustPower, each holding less than 1% of the shares.

Powerco

20. Powerco is an electricity lines business, whose distribution network includes lines in the Tauranga and Taranaki regions.
21. Powerco (the operating company) is 100% owned by Powerco NZ Holdings Limited. 42% of Powerco NZ Holdings Limited is owned by Babcock and Brown Infrastructure Limited (through a series of subsidiaries) and 58% is owned by two managed funds which are owned by Queensland Investment Corporation.
22. Powerco has nearly 27,500km of lines serving over 305,000 connected customers and conveying nearly 4,500 GWh of electricity annually.
23. TrustPower’s Kaimai and Patea hydro stations, and the Tararua wind farm, are all connected to Powerco’s network.
24. TrustPower is currently selling electricity to customers connected to Powerco’s network under an existing use of system agreement. Mr Tume has confirmed that this is on terms no more or less favourable than other electricity retailers’ use of system agreements for Powerco’s network. These other retailers include Genesis Energy, Meridian Energy, Mighty River Power, Contact Energy, King Country Energy, Bay of Plenty Electricity, Todd Energy, Simply Energy and Powershop.
25. Powerco purchases electricity for its own consumption from [].
26. Mr Tume has confirmed that the other existing directors of Powerco have no involvements with TrustPower and Infratil.

³ Tauranga Energy Consumer Trust.

MARK TUME'S APPLICATION

27. Mr Tume has applied, under section 81 of the EIR Act, for exemption from the requirement to comply with the EIR Act in respect of his potential prohibited involvements that would arise from his directorship of Infratil and Infratil's involvement in generation connected to Powerco's network, and his proposed directorship of Powerco's lines business.
28. The exemption is sought to enable Mr Tume to be appointed to the Board of Directors of Powerco, without being in breach of the EIR Act.

APPLICATION OF THE EIR ACT TO MR TUME

Involvements

29. The Commission has previously considered several applications from individuals who wished to become directors of both electricity lines and generation/sales businesses. In each case, the Commission granted exemption⁴ from the potential involvements in breach of the EIR Act, arising by way of the deemed material influence of a director of an electricity business. However, the present case is the first time the Commission has considered an application for exemption from the ownership separation provisions of the EIR Act, whereby the applicant (Mr Tume in this case) is not a director of an electricity business but is once removed as a director of a company that is a shareholder in an electricity business. Therefore, the Commission must reach a view as to the correct interpretation of "involved" under section 7 of the EIR Act, in these circumstances.
30. Section 7 of the EIR Act is provided for reference below:

7 Meaning of involved

(1) For the purposes of this Act, a person is involved –

- (a) in a line if the person conveys electricity by the line, or owns or operates, directly or indirectly, the line or any other assets used in connection with the line, either alone or together with its associates and either on its own or another's behalf;*
- (b) in any generation if the person generates electricity from the generator, or owns or operates, directly or indirectly, the generator or any other assets used in connection with the generator, either alone or together with its associates and either on its own or another's behalf;*
- (c) in selling electricity to a customer if the person sells to a customer either on its own or another's behalf;*
- (d) in any of the things referred to in the paragraphs (a) to (c) if the person –*
 - (i) carries on a business that does any of those things, either alone or together with its associates and either on its own or another's behalf; or*

⁴ But with certain conditions attached.

- (ii) *exceeds the 10% threshold in section 8 in respect of a business that does any of those things; or*
- (iii) *has material influence over a business that does any of those things.*

(2) *Involvement has a corresponding meaning.*

31. In his application, Mr Tume conceded that his proposed directorship of Powerco “would see him involved in a line.” However, he submitted that it was arguable that, for various reasons that do not need to be traversed here, his directorship of Infratil did not result in his involvement in generation or supply. His application for exemption was made to cover the contingency that the Commission would take the alternative view (which it has). That is, the Commission does consider that Mr Tume is currently involved in both generation and sales of electricity as a result of his directorship of Infratil and Infratil’s majority shareholding in TrustPower, when taken together.
32. The Commission considers that the scheme of section 7(1) is to set out how involvement can arise at each of three functional levels of electricity markets (excluding transmission). Distribution is covered by paragraph (a), generation by (b), and retailing by (c). Paragraph (d) is a provision having general application to each of paragraphs (a) to (c). It provides an elaboration of the principles pertaining to each of the categories of involvement described in (a) to (c). A person may be involved in each of the three functional levels if that person carries on the electricity business or exceeds the 10% threshold for control or equity rights over the electricity business, or has material influence over the electricity business.
33. Thus the Commission considers that Infratil:
 - is involved in generation because it indirectly owns, via its majority shareholding in TrustPower, generators and other assets used in connection with the generators; and
 - is involved in generation and selling electricity because it has more than 10% of the control and equity return rights in a business and has material influence over a business (TrustPower in both cases) that does the things in section 7(1)(b) and section 7(1)(c). Those things done by TrustPower are generation of electricity and ownership directly of generators and other generation assets and sale of electricity to customers.
34. Mr Tume's involvement in generation and selling arises through the fact that he is deemed to have material influence over TrustPower by virtue of section 11. Under section 11(2), Infratil (a person) has material influence over TrustPower (an electricity business), and another person (Mr Tume) has the powers referred to in various of the paragraphs (c) to (f) over Infratil⁵. Section 11 is couched in terms of influence arising where there exists the mere power to influence. Actual influence is not required to be established. Therefore, in the Commission’s view, Mr Tume is deemed by section 11(2) to also have material influence over the electricity business (TrustPower), notwithstanding Mr

⁵ For example, Mr Tume, would be expected to direct or instruct managers of Infratil (the first person) (paragraph (c)), he can exercise the powers of a director of Infratil (paragraph (d)), he can control the appointment or removal of managers of Infratil (paragraph (e)) and he has the power to influence a decision of Infratil that would ordinarily require more than 10% of the control rights (paragraph (f)).

Tume's submission to the contrary.⁶ Therefore, by virtue of section 7(1)(d)(iii), Mr Tume is involved in both generation and selling electricity.

Mr Tume's Potential Prohibited Involvements

35. Under section 17(2) of the EIR Act it is a contravention of Part 2 for a person to have an involvement that breaches the connected generation cap and/or the connected customers selling cap rules.

Application of the Connected Generation Cap Rule to Mr Tume

36. The connected generation cap is set out in section 17A of the EIR Act. Section 17A provides that the cap is breached if any of a person's connected generation with a capacity greater than 5 MW in total was commissioned before 20 May 2003, or a person's connected generation has a total capacity that exceeds the greater of 50 MW or 20% of the average of the maximum demand, in the immediately preceding 3 financial years, on the local network area.
37. The term "connected generation" is defined in section 3 of the EIR Act to mean "generation in which the person is involved that is connected to a line in which the person is involved, if the generation and the line are within the same local network area".
38. Section 17B describes the types of connected generation that do not count for the purposes of the connected generation cap rule. In particular, generation commissioned on or after 8 August 2001 if the electricity generated from it is produced only from renewable energy sources, is not counted for the purpose of section 17A.
39. TrustPower has [] MW of generation connected to Powerco's network that was commissioned prior to 20 May 2003.⁷ Therefore, TrustPower's connected generation by far exceeds the criteria of section 17A(1)(a) in the connected generation cap rule. As concluded above, Mr Tume is involved in that generation.
40. Accordingly, the Commission considers that, if appointed to the Board of Powerco, Mr Tume would breach the connected generation cap rule (section 17A(1)(a) of the EIR Act) and section 17(2)(a) of the EIR Act would apply to him, in respect of his involvements in Powerco's lines and Infratil's generation (via TrustPower). Consequently, Mr Tume would require exemption from section 17(2)(a) of the EIR Act.

Application of the Connected Customers Selling Cap Rule to Mr Tume

41. The connected customers selling cap is set out in section 17(C) of the EIR Act. Section 17(C) provides that the cap is breached if a person is involved in selling more electricity to connected customers within a local network area in a financial year, than the equivalent of the person's qualifying generation within the local network area.
42. The person's qualifying generation is the sum of the total annual nominal MWh capacity of the following generation (calculated as if the generation were operated at total nameplate capacity for 24 hours for 365 days per annum):

⁶ See paragraph 47(b) below.

⁷ See Appendix 1. Section 17B applies to exclude Stage 2 of the Tararua windfarm from being counted in for the purposes of the connected generation cap.

- (a) the person's connected generation counted for the purpose of the connected generation cap in section 17A;
 - (b) any connected generation referred to in section 17B(a), (b) or (c) in which the person has an involvement; and
 - (c) any generation referred to in section 17B (a) or (b) that is connected to the national grid, if:
 - (i) on application by or on behalf of the person, the Commission has determined, by notice in the *Gazette*, that the generation should be treated as being within the local network area of the lines in which the person is involved; and
 - (ii) the total capacity of all generation in which the person has an involvement does not exceed 100 MW.⁸
43. Thus, for the purposes of the customer selling cap rule, the generation from stage 2 of the Tararua windfarm is included in the calculation.
44. Finally, section 19 of the EIR Act describes the businesses and involvements to be disregarded under the EIR Act. However, none of the provisions in section 19 apply in this case.
45. In the last financial year, TrustPower sold [] GWh of electricity to customers connected to Powerco's network. As is shown in Appendix 1, the qualifying generation calculated for the purposes of Mr Tume's application is calculated as [] GWh. That amount exceeds the amount of electricity sold by TrustPower to customers connected to Powerco's network. Therefore, the Commission considers that if he were to be appointed to the Board of Powerco, Mr Tume would not breach the connected customers selling cap.
46. The amounts of connected generation and (more likely) connected customers selling by TrustPower might change in future. However, as matters stand at present, Mr Tume is not required to obtain an exemption from section 17(2)(b) of the EIR Act. In the event that circumstances changed⁹, he would need to either seek a variation to the exemption granted in this Decision or apply for a further exemption.

MR TUME'S SUBMISSIONS IN SUPPORT OF HIS APPLICATION

47. Mr Tume submitted that the granting of an exemption would not create incentives or opportunities to inhibit competition in the electricity industry because:
- (a) as a director of Infratil, Mr Tume is bound by a duty, under the Companies Act 1993, to make decisions in the best interests of Infratil. He would be under the same duty in respect of Powerco;
 - (b) Mr Tume is only one director on the Infratil Board, which has a majority of independent directors and, in any event, does not address matters relating to the operational details of TrustPower's business such as TrustPower's agreements with electricity distribution companies; and

⁸ This subparagraph (c) does not apply in this case.

⁹ For example, if TrustPower gained large customers connected to Powerco's network from competitors.

- (c) Powerco will require Mr Tume to not participate in discussions, or voting, on matters relating to TrustPower.
48. Mr Tume submitted that the granting of an exemption would not create incentives or opportunities to cross-subsidise generation activities from electricity lines businesses because:
- (a) Powerco and TrustPower have existing agreements relating to TrustPower's connected generation. These agreements are not due to expire in the near future. Powerco is unaware of any further TrustPower generation project that would connect to Powerco's network. Due to Powerco's requirement that Mr Tume absent himself from voting and discussion on TrustPower matters, Mr Tume will not be in a position to influence these agreements in any way;
 - (b) Powerco's electricity lines are subject to price control and information disclosure requirements under Part 4 of the Commerce Act. Even if Powerco was willing to attempt to cross-subsidise TrustPower's generation activities once Mr Tume was appointed to the Powerco Board, the Part 4 regulatory regime means Powerco would have minimal, if any, opportunity to do so;
 - (c) From a distribution /retail perspective, the companies are subject to use-of-systems agreements with respect to Powerco's supply of lines services to TrustPower. The only possible amendment Powerco envisages to these agreements is changes to reflect any model use-of-system agreement mandated by the Electricity Commission;
 - (d) As with Powerco and TrustPower's connected generation agreements, due to Powerco's requirement that Mr Tume absent himself from voting and discussion on TrustPower matters, Mr Tume will not be in a position to amend the use-of-system agreements in such a way that Powerco did not earn a commercial return on this supply, or TrustPower was favoured relative to other retailers. In fact, Powerco has previously committed to charge the same price to all retailers to which it supplies electricity; and
 - (e) To the extent that the Commission remains concerned that Mr Tume's appointment may give rise to any opportunities or incentives to inhibit competition or lead to cross-subsidisation of TrustPower's generation, the Commission could grant an exemption on the condition that, while Mr Tume is involved in connected generation, he shall not participate in any discussions or decision making by Powerco regarding matters that relate to or could affect the supply of connected generation by TrustPower to Powerco, or that could affect the supply or favour provision of electricity lines services by Powerco to TrustPower.
49. Mr Tume submitted that the granting of an exemption would not create a relationship between Powerco and TrustPower which is not at arm's length because the arm's length rules are already met by Powerco and TrustPower being separate and independent companies, and by Powerco and Infratil being separate and independent companies.

EXAMINATION IN TERMS OF THE COMMISSION'S CRITERIA

Relevant Markets

50. Mr Tume's potential prohibited involvements extend only to TrustPower's generation that is connected to Powerco's network. In the Commission's view, the potential for his involvements to harm the purposes of the EIR Act might arise from amongst other things:
- generators, other than TrustPower, might be prevented from connecting to Powerco's network or connecting on less favourable commercial conditions than apply to TrustPower;
 - electricity sellers, other than TrustPower, might be disadvantaged in respect of the commercial conditions in their use of system agreements with Powerco;
 - Powerco might require, as a condition of connection to its networks, that its customers purchase their electricity from TrustPower; and
 - less importantly, Powerco might favour TrustPower in respect of Powerco's electricity purchases for its own consumption.
51. The Commission is of the view that the relevant markets¹⁰ in this instance are the national electricity generation and wholesale market,¹¹ the relevant electricity retail markets,¹² and the electricity distribution market that corresponds with Powerco's electricity distribution network.¹³

Question 1: 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 inhibit competition in the electricity industry?

52. The Commission has examined the facts of this case, and is of the view that any incentives or opportunities to inhibit competition in the electricity industry that would be created by the granting of an exemption in respect of the potential prohibited involvements, could be effectively addressed by limiting Mr Tume's participation as a director of both Infratil and Powerco, in matters that relate to:
- the connection of TrustPower's generators to both Powerco's network and any other lines company's network;
 - TrustPower's use of system agreement in respect of Powerco's network and any other lines company's network;

¹⁰ Other markets in the electricity industry, for example the electrical construction and maintenance market and the market for reticulation of new subdivisions, do not appear to be relevant to this application for exemption.

¹¹ For a discussion of electricity generation market definition see Commerce Commission, *Decision 340: Transalta Corporation of Canada / Contact Energy*, 12 February 1999 and Commerce Commission, *Decision 491: Contact Energy Limited / Natural Gas Corporation Holdings Limited*, 04 February 2003.

¹² For a discussion of relevant electricity retail markets definition see Commerce Commission, *Decision 517: Dr Keith Turner*, 17 March 2004 and Commerce Commission, *Decision 547: Mr Wayne Boyd*, 31 March 2005.

¹³ For discussion of electricity distribution market definition see Commerce Commission, *Decision 345: United Networks Limited / Transalta New Zealand Limited*, 11 March 1999 and Commerce Commission, *Decision 299: Holdco (Mercury Energy Ltd and Utilicorp) / Power New Zealand Ltd*, 27 June 1997.

- other electricity sellers use of system agreements in respect of Powerco's network;
 - the supply of electricity by any electricity seller (including TrustPower) to any of Powerco's network customers; and
 - the supply of electricity by TrustPower to Powerco.
53. Therefore, the Commission considers that any exemption granted should be subject to the condition that Mr Tume be prohibited from participating in any discussions or decision making that relate to or could affect the above list of matters.

Conclusion on Question 1

54. The Commission is of the view that, in respect of the national electricity generation and wholesale market, the relevant electricity retail market, and the local electricity distribution market corresponding to Powerco's network, the granting of an exemption in this case, subject to the above condition, is unlikely to create incentives or opportunities to inhibit competition.

Question 2: Incentives or Opportunities to Cross-subsidise Generation or Retail Activities

Would the Commission, by granting an exemption in respect of a business or involvement or interest, create incentives or opportunities to cross-subsidise generation or retail activities from electricity lines activities?

55. The Commission considers that if a lines business is also involved in generation or sale of electricity, it would have the opportunity to cross-subsidise the generation or selling activities, should it choose to do so. Cross-subsidisation could take a number of forms. It may be that the lines business would meet costs which more properly lie with the generation or retail side of the business. It may be that common costs would all be attributed to the lines business. It may be that the lines business would provide capital to the generation or retail side of the business at less than its true cost. It may be that a generation or retail project would be funded in a way which weakens the financial stability of the lines business.
56. The Commission considers that the potential for cross-subsidisation of generation activities is of particular concern where a generator has the potential to connect generation to a local distribution network. In this case, Mr Tume could influence Powerco to connect TrustPower's generation to Powerco's network on more favourable commercial terms than other generators by Powerco reducing its standard charges for same to TrustPower.
57. The Commission considers that the potential for cross-subsidisation of retail activities is of particular concern where a retailer has the potential to sell electricity to customers connected to a local distribution network. Again, given TrustPower currently sells approximately []% of the total electricity conveyed across Powerco's network under an existing use of system agreement, Mr Tume could influence Powerco to reduce charges only to TrustPower, for use of its network.
58. Again, the Commission considers that, providing Mr Tume does not participate in any future discussion or decision making that relates to the list of matters in paragraph 52, Powerco would have no incentives or opportunities to cross-subsidise TrustPower's generation or retail activities from its lines business.

Conclusion on Question 2

59. The Commission considers that, in this case, the granting of an exemption subject to the condition above is unlikely to create incentives or opportunities to cross subsidise between lines activities and generation or retail activities.

Question 3: Requirement for Corporate Separation and Compliance with arm's-length and use-of-system rules

Where applicable, would the Commission permit, by granting an exemption in respect of a business or involvement or interest, a relationship between a business that has involvement in electricity lines and a business that has involvement in electricity generation or retail, where those relationships may not otherwise be at arm's length?

60. Section 17E of the EIR Act requires that, where a business is a “connected electricity business”, it must comply with the corporate separation requirements and arm's-length rules. It must also comply with the use-of-systems agreement rules in section 17F of the EIR Act.
61. Section 17D states that a business is a connected electricity business if the business, or a person involved in the business, has an involvement in more than 10 MW of connected generation. Section 3 defines connected generation as meaning generation in which a person is involved that is connected to a line in which the person is involved, if the generation and the line are in the same network area.
62. In this case, TrustPower has [] MW of generation connected to Powerco's network and, therefore, Mr Tume is involved in a connected electricity business and the requirements for corporate separation and compliance with the arm's-length and use-of-system agreements rules must be met. As Powerco, TrustPower and Infratil are separate and independent companies, the requirement for corporate separation is met.
63. As to the required compliance with the arm's-length rules and the use-of-systems agreements rule, these are such that it would be difficult for the Commission, as an external enforcement agency to determine whether or not Mr Tume, Infratil, and TrustPower are complying with the arm's-length rules and whether or not Mr Tume and Powerco are complying with both the arm's-length and the use-of-system agreements rules. The Commission, therefore, requires as a condition of the exemption it will grant Mr Tume, for him to provide to the Commission an annual declaration of compliance stipulating that, to the best of his knowledge, he, Infratil, TrustPower and Powerco are complying with the arm's-length rules and the use-of-systems agreements rules as applicable. The first such declaration shall be by 31 October 2010 and annually thereafter.

Conclusion on Question 3

64. The Commission by granting exemption from section 17(2)(a) does not exempt Mr Tume from compliance with the arm's-length or use-of-systems agreements rules. The Commission considers that Mr Tume, Infratil, TrustPower and Powerco must comply with those rules as applicable in respect of Mr Tume's prohibited (but exempted) involvements.

Conclusion in Respect of the Commission's Criteria

65. The Commission considers that, provided Mr Tume complies with the conditions in the Notice of Exemption, the granting of an exemption to him from the application of section 17(2)(a) is unlikely to create incentives or opportunities to inhibit competition in the electricity industry and is unlikely to result in any material increase in the opportunities or incentives to cross-subsidise electricity generation or sales from electricity lines activities.
66. Accordingly, the Commission determines to grant such an exemption with conditions to Mr Tume.
67. The Commission in previous decisions on similar applications for exemption has imposed a condition on the director in the position of Mr Tume that he or she should not participate in any discussions or decision making by the relevant lines company concerning the connection of any generators to the lines company's network.
68. Mr Tume has resisted the imposition of that condition for the following reasons:
 - [];
 - []; and
 - [].
69. The relevant condition is designed to prevent a director of a lines company who is (like Mr Tume) also a director of a generation company from using his or her influence to obstruct the connection of competing generators to the lines.
70. In this case, the Commission notes that the Powerco Board is made up of representatives of Babcock and Brown and the Queensland Investment Corporation or representatives recommended by those two shareholders. It seems to the Commission inherently unlikely that those directors as a group would have any incentive to favour TrustPower over other generators who could provide Powerco with on-going revenue streams if they were connected to its network.
71. In any event, Mr Tume must comply with the Arm's-length rules. Under rule 1 he has a duty to ensure that Powerco and TrustPower operate at arms length. Amongst other things Mr Tume must also ensure that Powerco does not discriminate against other generators in favour of TrustPower (rule 4).
72. On these facts, the Commission does not consider that Mr Tume will have any ability, as a single director of Powerco, to influence Board decisions in favour of TrustPower or against other generators. Therefore, it considers the relevant condition, previously applied in similar cases, is unnecessary in the case of Mr Tume.

THE COMMISSION'S DETERMINATION

73. The Commission determines to grant an exemption to Mark Tume from section 17(2)(a) of the EIR Act, in respect of the prohibited involvements outlined in this Decision, subject to the conditions specified in the attached Notice of Exemption.

Dated this day of November 2009

Dr. Mark Berry

Chair

APPENDIX 1: TrustPower's Generation Connected to Powerco's Network

Generation	Annual output (GWh)		Nameplate capacity (MW)	Commissioned
Kaimai	[]	Kaimai 5 Station	0.3	1994
		Lloyd Mandeno	16	1972
		Lower Mangapapa	5.6	1979
		Ruahihi	20	1983
Patea	[]		31.4	1983/84
Mangorei	[]		4.5	1931
Motukawa	[]		4.6	1927
Tararua Windfarm	[]	Stage 1	34	1999
Tararua Windfarm	[]	Stage 2	34	2004
Total			150.4 MW	
*24 hours			3609.6 MWh	
*365 days			1,317,504 MWh (1,317.504 GWh)	

NOTICE OF EXEMPTION

The Commerce Commission (Commission), pursuant to section 81 of the Electricity Industry Reform Act 1998 (the EIR Act), exempts Mark Tume from compliance with section 17(2)(a) of the EIR Act in respect of the involvements (as that term is defined in the EIR Act) with Infratil Limited and Powerco Limited as outlined in the Commission's Decision 682 on his application for exemption.

1. Whilst Mark Tume is involved with both Infratil Limited and Powerco Limited, he shall not participate in any discussions or decision making by Infratil Limited and/or Powerco Limited regarding any of the matters listed below:
 - the connection of TrustPower Limited's generators to both Powerco Limited's network and any other lines company's network;
 - TrustPower Limited's use of system agreement in respect of Powerco Limited's network and any other lines company's network;
 - other electricity sellers use of system agreements in respect of Powerco Limited's network;
 - the supply of electricity by any electricity seller (including TrustPower Limited) to any of Powerco Limited's network customers; or
 - the supply of electricity by TrustPower Limited to Powerco Limited.

In addition, he shall not disclose the outcomes of any discussions or decision making by Powerco Limited on these matters to Infratil Limited, or any shareholder, director or staff member of Infratil Limited (and vice versa).

2. Mark Tume shall provide an annual declaration of compliance with arm's-length and use-of-system agreements rules to the Commission. Mr Tume shall declare in writing that, to the best of his knowledge, he, Infratil, TrustPower and Powerco are complying with the arm's-length Rules and the use-of-systems agreements rules. The first such declaration shall be by 31 October 2010 and annually thereafter.
3. Mark Tume will confirm to the Commission, in writing, that the prohibited involvements to which this exemption applies have ceased within one calendar month of the prohibited involvements ceasing to exist;
4. This exemption expires when the Commission publishes on its website Mark Tume's written confirmation that his prohibited involvements have ceased, unless any variation or earlier revocation in terms of section 81(5) occurs before that event; and
5. This exemption is specific to the prohibited involvements created through Mark Tume's involvements in Powerco Limited and Infratil Limited. It does not extend to any other interest or existing or future prohibited involvements of Mark Tume.

The exemption takes effect from the date of publication of this notice in the *New Zealand Gazette*.

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

Dated this day of November 2009

Dr. Mark Berry
Chair