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5 December 2002

Mr John Belgrave
Chair
Commerce Commission
PO Box 2351
Wellington

Dear Mr Belgrave,

PROCESS ISSUES

Background

1. By virtue of section 57G of the Commerce Act, the Commission has a duty to consult with participants in the electricity distribution and transmission markets, and with consumers, before it sets thresholds. A similar obligation exists under section 57ZE in relation to the review of asset valuation methodologies, in respect of which the Commission is currently undertaking a consultation process.
2. The Commission released a discussion paper on 21 March 2002 on threshold design issues. In paragraph 8.86 of this discussion paper the Commission sets out four possible threshold options. This discussion paper also sets out various factors that the Commission would take into account in choosing between these options (paragraphs 8.89 to 8.92). The Commission expressed no clear preference for the approach it proposed to take. This discussion paper was very much in the nature of an issues paper.
3. Wide-ranging submissions were made by industry participants, and other interested parties, in response to this discussion paper. These submissions recommended, inter alia, that the Commission should modify certain of the four possible thresholds outlined in the discussion paper. Some submitters also put forward thresholds which were not described in the Commission's discussion paper.
4. On 1 October 2002 the Commission released a further discussion paper on asset valuation methodologies. The media release which accompanied the release of this report (*Media Release 2002/45*) was

suggestive of a convergence of this asset valuation methodology exercise with the earlier threshold discussion paper. The Commission advised that in December this year it would “release a high-level paper outlining the Commission’s final decisions on the form of the thresholds” alongside the paper “announcing the results of the review of asset valuation methodologies”. The Commission also advised that it “will further consult on the implementation details of the thresholds early in 2003”.

5. Prior to the commencement of the current conference, the Commission commented further on these issues in its letter dated 18 September 2002. On the question of the setting of thresholds this letter advised that “it would be appropriate for the Commission to set its view as to the general thresholds” and that the “Commission’s process will then consider particular aspects of thresholds with the objective that the thresholds be published by 31 March 2003.” This letter also advised that “for lines companies to assess the impact of thresholds on their performance (even if only broadly), the Commission considers the outcome of RAVM should be known.”
6. The Commission has not indicated its preferred approach to threshold design. The 21 March 2002 discussion paper was non-committal on the issue and at no time since the release of this discussion paper has the Commission elaborated further on its view on thresholds.
7. It follows that there is currently significant uncertainty as to what the Commission is proposing in the design of its preferred threshold. The threshold could be any one of the four options suggested in the 21 March 2002 discussion paper. It could be a mixture of these options. It could be one of the alternate options submitters put forward at the thresholds conference, with or without modification. We do not know.
8. Similar uncertainties surround the current review of the Commission’s asset valuation methodology discussion paper because no preferred view has been put forward by the Commission. Further, the absence of a Commission proposal on thresholds means that the asset methodology consultation currently being undertaken is occurring in the abstract.
9. It now appears from the statements noted above, that the Commission proposes to reach its final decision on these issues before the end of this year, without further consultation.

Consultation Principles

10. The Court of Appeal, in *Wellington International Airport Ltd v Air New Zealand* [1993] NZLR 671, has accepted that the leading authority as to

the requirement for consultation is *Port Louis Corporation v Attorney-General of Mauritius* [1965] AC 1111.

11. The following basic principles emerge from the decision of the Privy Council in *Port Louis Corporation*:
 - 11.1 It must be made known what is proposed. The proposal needs to be clearly stated (pp 1124, 1131);
 - 11.2 Those being consulted must be given a reasonably ample and sufficient opportunity to express their views or to point to problems or difficulties (p 1124). In the present context, in our opinion, this obligation requires that the proposal should be set out in sufficient detail so that those being consulted are able to understand its rationale. Meaningful consultation requires that parties be able to express views on the analysis that may favour one option over another; and
 - 11.3 The decision maker must of course approach the consultation with a mind that is genuinely open to alternatives.

Assessment of Processes to Date

12. The Commission, thus far, has only invited submissions in relation to wide-ranging issues papers. This is understandable, and appropriate, given the limited guidance provided in the legislation and the “newness” of the issues involved under Part 4A of the Commerce Act.
13. However, at no point has the Commission put forward a clear proposal of its intended threshold. For this reason, the Commission has not yet engaged in proper consultation, as required under section 57G. Similarly, the discussion paper on asset valuation methodologies, which the Commission is now linking to the thresholds exercise, contains no clear outline of the Commission’s current position. Orion agrees that the two are necessarily linked, and, should the Commission include a threshold linked to an asset valuation, there cannot be a meaningful threshold proposal until the Commission is able to present the proposal that incorporates a proposed asset valuation methodology.
14. It follows that:
 - 14.1 The Commission has not yet made known, with sufficient clarity, what is proposed on the question of thresholds and asset valuation methodologies.
 - 14.2 In order to discharge its duty to consult under sections 57G and 57ZE, the Commission must now make known to the industry participants, and to other interested persons, the thresholds and

asset valuation methodology it proposes to adopt. The Commission must then give sufficient time for submissions on this proposal.

- 14.3 In the course of our presentation to the Commission at the thresholds conference (21 August 2002, pp 46-47 of the transcript), and in our submission of 11 November 2002 on asset valuation methodologies, we invited the Commission, at this stage, to issue a proposal in the form of a draft determination rather than a final decision. This draft determination process was suggested as a way to comply with the consultation process requirements just described.
- 14.4 If the Commission now proceeds to issue a final decision on these matters, as indicated in *Media Release 2002/45* and the 18 November letter, then proper consultation processes will not have been followed and the Commission's decision will be reviewable.

Yours sincerely

Chris Laurie
Managing Director