



COMMERCE COMMISSION

**Treatment of Consumer-owned Electricity Distribution  
Businesses under the Initial Default Price-Quality Path**

Network Performance Branch

Commerce Commission

Wellington

NEW ZEALAND

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## Background

1. As suppliers of electricity lines services, EDBs are subject to default/customised price-quality regulation under subpart 9 of Part 4 of the Commerce Act 1986 (“the Act”). Electricity distribution businesses (“EDBs”) that meet the consumer-owned criteria set out in section 54D of the Act (“consumer-owned EDBs”) are exempt from default/customised price-quality regulation.<sup>1</sup>
2. This paper sets out the Commerce Commission’s (“Commission”) treatment of EDBs that meet the consumer-owned criteria in relation to the default price-quality path that applies from 1 April 2009 to 31 March 2010 (“Initial DPP”). It includes the Commission’s interpretation of the relevant statutory provisions, and assessment and notification requirements for EDBs.
3. The Commission has taken the views expressed by interested parties in submissions<sup>2</sup> and correspondence on previous consultation papers into account when forming its views. Previous consultation papers include:
  - the *Proposed Approach to Consumer-owned Electricity Distribution Businesses under the Initial Default Price-Quality Path*, published on 16 March 2009; and
  - the *Treatment of Consumer-owned Electricity Distribution Businesses under the Initial Default Price-Quality Path* (the previous version of this paper), published on 11 August 2009.

## Interpretation of Section 54D

4. Section 54D(1) provides that:

### 54D Definition of consumer-owned

- (1) In this subpart, unless the context otherwise requires, a supplier is **consumer-owned** if it is a supplier that meets the following criteria:
  - (a) all the control rights and all the equity return rights (within the meaning of section 3 of the Electricity Industry Reform Act 1998) in the supplier are held by 1 or more customer trusts, community trusts, or customer co-operatives; and
  - (b) the trustees of each customer trust or community trust, or the directors of each customer co-operative, as the case may be, that is referred to in paragraph (a) are elected solely by the persons who are consumers of the supplier, and at least 90% of the persons who are consumers of the supplier at the time of the election are eligible to vote in those elections; and
  - (c) at least 90% of the persons who are consumers of the supplier as at an income distribution resolution date benefit from that income distribution; and

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<sup>1</sup> Commerce Act 1986, section 54G.

<sup>2</sup> Copies of these submissions are available at <http://www.comcom.govt.nz/IndustryRegulation/Electricity/PriceQualityPaths/consumerowned.aspx>.

- (d) the supplier has fewer than 150 000 ICPs.
5. Interpreting section 54D(1)(b) is a complex exercise given that there are various scenarios that happen in practice in a number of trusts that are not explicitly addressed by the Act. For instance, the Act does not explicitly address the scenario where the number of nominations is less than or equal to the number of vacancies, or where a casual vacancy arises between scheduled elections. The Commission has carefully considered the relevant provisions, the statutory context and the reasoning for consumer-owned exemptions in reaching its views on these scenarios and in forming its interpretation of section 54D(1)(b). The Commission has also carefully considered submissions and correspondence it has received from interested parties on these matters.
  6. The Explanatory Note to the Commerce Amendment Bill as introduced stated that “the reason for this relatively light-handed regime is because consumers, as owners, are able to ensure that the business acts in their interests”<sup>3</sup>, and with regard to 100 percent consumer trust-owned businesses, “in principle the case for economic regulation is relatively weak where the customers are the owners of the firm”.<sup>4</sup>
  7. Section 54D(1)(b) requires the trustees (or directors) to be “elected” solely by consumers and that at least 90 percent of the consumers were eligible to vote in the election of those trustees. The Commission considers that this provision indicates that trustees (or directors) must be elected, not appointed. The Commission also notes that the reference to “appointment” was deleted from the definition of “consumer-owned” by the Select Committee that considered the Bill.
  8. The Commission also considers that it is implicit under section 54D(1)(b) that each consumer has an equal vote. The legislation specifies only that voting rights attach to persons who are consumers. The term “consumer” is defined in section 54D(2) as having the same meaning as in section 2(1) of the Electricity Act 1992,<sup>5</sup> and includes any person listed on an electoral roll as a resident of an address that consumes that electricity.<sup>6</sup> The Act requires that at least 90 percent

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<sup>3</sup> Explanatory note to the Commerce Amendment Bill (201-1), Government Bill, as introduced to the House of Representatives, Wellington, 13 February 2008, p. 8.

<sup>4</sup> Explanatory note to the Commerce Amendment Bill (201-1), Government Bill, as introduced to the House of Representatives, Wellington, 13 February 2008, p. 31.

<sup>5</sup> Under section 2(1) of the Electricity Act 1992, “consumer”—

- (a) Means any person who is supplied, or who applies to be supplied, with electricity; but
- (b) Does not include any electricity generator or any electricity distributor or electricity retailer, except where the electricity generator or, as the case may be, the electricity distributor or electricity retailer is supplied, or applies to be supplied, with electricity for its own consumption and not for the purposes of resupply to any other person.

<sup>6</sup> The Commission notes that the Act does not specify any particular electoral roll or how the electoral roll should be constructed. The Commission does not consider it necessary to impose a definition that may restrict the meaning of “electoral roll”.

of all consumers of electricity supplied by the “consumer-owned” supplier are eligible to vote for the trustees of that supplier.<sup>7</sup>

9. Parliament has not explicitly provided how voting rights should be divided among these consumers, however, adopting a purposive approach in interpreting section 54D(1)(b) the Commission considers that equal voting rights in the normal democratic sense applies. Had Parliament intended differential voting based on, for example, volume of electricity supplied, the Commission would have expected Parliament to have made an explicit provision for such voting given that voting rights are central to the ability of consumers to influence a 100 percent consumer trust-owned supplier.
10. In presenting its views below, the Commission has tried to give effect to the intent of consumer-ownership exemptions and to the integrity of the democratic process by which consumer representatives are elected.
11. In the Commission’s view, the criterion in section 54D(1)(b) is satisfied if:
  - each trustee of a trust or community trust, or director of a customer cooperative, has been elected by the consumers of the supplier; and
  - no one other than a consumer voted in the election; and
  - at least 90 percent of consumers must have been eligible to vote with each consumer having an equal vote.
12. The Commission has considered a number of scenarios and has formed the following views:
  - (i) The circumstance where the number of nominations for an election is equal to or less than the number of positions, and the nominees are declared elected without an election being held, reasonably meets the criterion in section 54D(1)(b). In this scenario the Commission is satisfied that the electoral process has been undertaken and that although an election was not held, those appointed to the positions of trustees may be considered elected for the purposes of section 54D(1)(b);
  - (ii) The circumstance where the next highest polling candidate is declared elected (at the time of the election), as the highest polling candidate is unable to fill the elected position, reasonably meets the criterion in section 54D(1)(b). The Commission is satisfied that the electoral process has also been undertaken in this scenario;

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<sup>7</sup> The Commission considers that this means that not more than 10 percent of consumers of the supplier at the time of the election were not eligible to vote for any reason, including:

- (a) for not being connected to the supplier’s network within a defined district; or
- (b) failing to satisfy a qualifying period; or
- (c) failing to appear on a qualifying roll; or
- (d) as a result of requesting not to be treated as consumers.

- (iii) The use of ward-based electorate voting<sup>8</sup> may reasonably meet the criterion in section 54D(1)(b) in some circumstances, but the Commission will assess this reasonableness on a case-by-case basis with regard to the following four principles (“Ward Principles”):
- (a) at least 90 percent of the persons in a ward who are consumers of the supplier at the time of the election are eligible to vote in the election of all trustees/directors of that ward;
  - (b) ward boundaries are to provide for effective and fair representation of all consumers of the supplier, including that the number of consumers per trustee/director is approximately equal in each ward;<sup>9</sup>
  - (c) wards are based on the number of consumers, not volume of electricity supplied; and
  - (d) ward boundaries are reviewed in consultation with all consumers of the supplier;
- (iv) The appointment of a trustee/director by the remaining trustees/directors, or by a committee wholly or partly elected by consumers, does not meet the criterion in section 54D(1)(b). The Commission is of the view that the intention of section 54D(1)(b) is that at least 90 percent of consumers must have the right to vote and that each consumer must have an equal right to vote. The Commission is of the opinion that this is not the case when a trustee/director is appointed;
- (v) The appointment of a trustee/director to take up the position of a casual vacancy does not meet the criterion in section 54D(1)(b). This person would be replacing a person declared elected rather than filling a vacancy at the time of the election (as in the case in scenario (ii) above). The Commission has considered all of the circumstances put to it by submitters with regard to this scenario. The Commission has also considered the possible restrictions that could be put on the appointment of casual vacancies, as suggested by submitters. The Commission is of the view that allowing the appointment of trustees to casual vacancies is inconsistent with, and would not satisfy, the criterion in section 54D(1)(b). This includes the appointment of a trustee/director (with or without restrictions) who was the next highest polling candidate at the time the vacating trustee/director was elected. Where a casual vacancy occurs, that position may be left vacant until an election is held; and
- (vi) Advisory trustees that do not have any decision-making role have no bearing on whether a supplier meets the criterion of section 54D(1)(b).

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<sup>8</sup> Ward-based voting systems divide an electorate into separate electoral districts, with the consumers in each separate district having the opportunity to vote for their representative(s) on the wider trust (i.e., not all the consumers within an electorate are eligible to vote for every trustee/director).

<sup>9</sup> For example, under most circumstances the number of consumers per trustee/director should not differ by more than 10 percent.

The Commission considers that the role of advisory trustees is such that whilst they provide advice to the trust that may result in a decision being made, advisory trustees do not have a direct decision-making role.

## **Assessment and Notification Requirements**

### ***General Compliance Requirement for EDBs for the Initial DPP***

13. Within 35 working days following the assessment date (31 March 2010), each EDB is required to submit to the Commission either:
  - (i) a compliance statement in accordance with the Commerce Act (Electricity Distribution Thresholds) Notice 2004 (“Notice”), which is deemed to be a section 52P determination under section 54J(2) of the Act; or
  - (ii) the statutory declaration attached at Appendix A (completed in its entirety, without amendment or exception) demonstrating that the EDB has met the Commission’s view of the consumer-owned criteria in section 54D of the Act.<sup>10</sup>

### ***EDBs that become Consumer-owned during the Initial DPP***

14. In accordance with paragraph 13 above, each EDB that becomes consumer-owned during the Initial DPP is required to submit to the Commission the statutory declaration attached at Appendix A.
15. The Commission intends to invoke clause 7(9)(a)(iii) of the Notice for any EDB that becomes consumer-owned during the Initial DPP. This will exempt the EDB from submitting a compliance statement for the portion of the Initial DPP that the statutory declaration does not apply.
16. An EDB which considers that they may merit such an exemption should notify the Commission in writing as soon as practicable following the EDB’s change in status.

### ***Ward-based Electorate Voting Clarification***

17. If an EDB/trust uses, or proposes to use, a ward-based electorate voting system, and considers that it meets all criteria under section 54D(1), the EDB/trust may seek clarification from the Commission as to whether the ward-based electorate voting system would mean, in the Commission’s view, that the EDB is consumer-owned.

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<sup>10</sup> The Commission is not aware of any EDBs that are customer cooperatives, as defined under section 54D(2). Hence, the statutory declaration has been drafted for customer/community trusts. Should the Commission become aware of a customer cooperative, an appropriate statutory declaration will be provided.

18. A clarification request from an EDB must:
- (i) be able to demonstrate, with any necessary supporting information or documentation, that its ward-based electorate voting system is consistent with each of the Ward Principles (set out in paragraph 12(iii));
  - (ii) include a director's certificate that certifies, having made all reasonable enquiry, to the best of the director(s) knowledge and belief, all information and documentation supplied to the Commission for the purposes set in paragraph 18(i) is true and accurate; and
  - (iii) be submitted to the Commission at any time prior to the assessment date.
19. The Commission's decision on a clarification request will be notified to the EDB as soon as practicable.
20. Where the Commission is satisfied that the use of a ward-based electorate voting system would be consistent with section 54D(1) of the Act, notification will include an alternative statutory declaration that the EDB must submit within 35 working days following the assessment date.

### **Record of Consumer-owned EDBs**

21. As soon as practicable following the end of the Initial DPP, the Commission will publish a list of EDBs that have provided completed statutory declarations.



## **Appendix A:**

### Statutory Declaration

## STATUTORY DECLARATION THAT A SUPPLIER IS CONSUMER-OWNED

*For the purposes of section 54D of the Commerce Act 1986 (“the Act”)*

*For the period* (insert date) *to 31 March 2010*

I, (insert full name),  
of

(insert place of abode and occupation),

solemnly and sincerely declare that –

1. I am the chairperson of trustees/a trustee\* of  
(insert name of trust) (the “Trust”);
2. Attached to this declaration is a complete copy of the current trust deed of the Trust;
3. At the date of this declaration, –
  - 3.1 the Trust –
    - (a) is a community trust/customer trust\* (as defined in section 54D(2) of the Act);
    - (b) is an income beneficiary/shareholder\* in  
(insert name of supplier) (the “Supplier”); and
    - (c) holds –
      - (i) all the control rights (as defined in section 3 of the Electricity Industry Reform Act 1998) in the Supplier; and
      - (ii) all the equity return rights (as defined in section 3 of the Electricity Industry Reform Act 1998) in the Supplier;
  - 3.2 other than any advisory or custodian trustees (consistent with section 49 and 50 of the Trustee Act 1956) who do not hold any decision-making powers –
    - (a) all the trustees of the Trust for this period were elected; and
    - (b) none of the trustees of the Trust for this period were appointed by other trustees, a committee, or anyone else;
  - 3.3 other than any advisory or custodian trustee referred to in paragraph 3.2, each of the trustees of the Trust for this period –
    - (a) was elected only by consumers as defined in section 54D(2) of the Act (“Consumers”) of the Supplier at the time of the election and by no other person; and



## EXPLANATORY NOTE

### *Drafting Notes*

1. The period to which this statutory declaration relates should be 1 April 2009 to 31 March 2010, unless a Supplier was consumer-owned for only part of that period.
2. Paragraph 2 – other documents or information, in addition to the current trust deed of the Trust, may also be appended in support of the declaration.
3. Paragraph 3.3(a) –
  - (a) the definition of “consumer” in section 54D(2) of the Act includes “...any person who is listed on an electoral roll as a resident of an address that consumes the electricity in question”. The Act does not specify any particular electoral roll or how the roll should be constructed.
  - (b) for the avoidance of doubt, this paragraph means trustees were elected only by persons who, at the time of the election, –
    - i. were supplied, or had applied to be supplied, with electricity by the Supplier; but
    - ii. were not electricity generators, distributors, or retailers unless consuming the electricity supplied by the Supplier for their own consumption (consistent with section 2 of the Electricity Act 1992); and/or
    - iii. were listed on an electoral roll as the resident of an address that consumes the electricity supplied by the Supplier (consistent with section 54D(2) of the Act).
4. Paragraph 3.3(b)(i) – for the avoidance of doubt, this means that not more than 10% of the Consumers of the Supplier at the time of the election were not eligible to vote for any reason, including:
  - (a) for not being connected to the Supplier’s network within a defined district; or
  - (b) failing to satisfy a qualifying period; or
  - (c) failing to appear on a qualifying roll; or
  - (d) as a result of requesting not to be treated as consumers.
5. This statutory declaration does not apply to Trusts that use a ward-based voting system to elect trustees. Trusts that use, or propose to use, a ward-based voting system must obtain an alternate form of statutory declaration from the Commission.

### ***Relevant Statutory Definitions***

6. **Section 54D(2) of the Commerce Act 1986** provides as follows:

(2) In this section, unless the context otherwise requires,—

**community trust**, in relation to a supplier, is a trust in respect of which—

- (a) at least 90% of the income beneficiaries comprise persons who are a class or classes identified by reference to their domicile or location or operation within the geographic area or areas of operation of the supplier; and
- (b) at least 90% of its income distributions are paid to those beneficiaries or for purposes related to that geographic area or areas

**consumer** has the same meaning as in section 2(1) of the Electricity Act 1992, and includes, for the purposes of references to the election of trustees in this section and section 54H, any person who is listed on an electoral roll as a resident of an address that consumes the electricity in question

**customer trust**, in relation to a supplier, means a trust in respect of which—

- (a) at least 90% of the income beneficiaries comprise persons who are a class or classes identified by reference to any of—
  - (i) the person's connection to the lines of the supplier:
  - (ii) the person's receipt of electricity from the supplier:
  - (iii) the person's liability for payment for supply of electricity from the supplier:
  - (iv) the person's liability for payment for the connection to the lines of the supplier:
  - (v) the person's liability for payment for line services supplied by the supplier; and
- (b) at least 90% of its income distributions are paid to those beneficiaries

**ICP** means a point of connection on a local or an embedded network at which a retailer supplies electricity to a consumer

**income distribution resolution date** means the date that a supplier, or the trust or cooperative that owns a supplier, as the case may be, resolves to make an income distribution to beneficiaries.

7. **Section 3 of the Electricity Industry Reform Act 1998** provides that:

**Control right** has the same meaning as in section 9

**Equity return right** has the same meaning as in section 10

8. **Section 9 of the Electricity Industry Reform Act 1998** provides the meaning of “control right”. Section 9 is as follows:

9. Meaning of “control rights”

- (1) For the purposes of this Act, a “control right” means a voting right attaching to a voting security.

- (2) A person has a control right under this Act if the person would have a relevant interest, under sections 5 to 5B of the Securities Markets Act 1988, in the voting securities that confer that right,—

(a) If “voting security”, in relation to a body, meant a security of the body which confers a right to vote at meetings of members (whether or not there is any restriction or limitation on the number of votes that may be cast by or on behalf of the holder of the security); and includes a security which, in accordance with the terms of the security, is convertible into a security of that kind; and

(b) If references in those sections to a number or percentage of voting securities were a reference to the number or percentage of the votes conferred by those securities.

9. **Section 10 of the Electricity Industry Reform Act 1998** provides the meaning of “equity return right”. Section 10 is as follows:

10 Meaning of “equity return rights”

- (1) For the purposes of this Act, a person has an “equity return right” in relation to a business if the person has a right or entitlement or expectancy to receive equity returns, directly or indirectly, of the business.

- (2) “Equity returns” means—

(a) Profits of the business; or

- (b) Distributions from the business; or
  - (c) Other equity returns from the business.
- (3) “Other equity returns”—
  - (a) Means a benefit derived, directly or indirectly, from a business which represents, or is calculated by reference to, or is determined by,—
    - (i) A share in or proportion of its capital; or
    - (ii) Its surplus or residual economic value (after satisfying prior contractual claims); or
    - (iii) Its profitability or other indicator of its success; but
  - (b) Does not include (for the avoidance of doubt) a right or entitlement to interest on debt calculated at general market rates prevailing at the time of the loan agreement, or fluctuating in accordance with a formula which applies general market rates prevailing from time to time.
- (4) In respect of equity return rights for which percentage entitlements are not readily calculable for any reason, the persons that hold or may hold them and the amounts are to be determined in accordance with any method set out in regulations.
- (5) A person is deemed to have a percentage of the equity return rights held by another person in a business if the first person has, or is one of 2 or more associates who together have, more than 10% of the equity return rights in the second person.
- (6) The percentage of rights held by a person in another person is calculated as follows:

$$a = b \times c$$

where-

a is the percentage to be determined

b is the percentage of the equity return rights held by the first person in the second person

c is the percentage of the equity return rights held by the second person in the business.

10. **Section 2(1) of the Electricity Act 1992** provides as follows:

**Consumer –**

- (a) Means any person who is supplied, or who applies to be supplied, with electricity; but
- (b) Does not include any electricity generator or any electricity distributor or electricity retailer, except where the electricity generator or, as the case may be, the electricity distributor or electricity retailer is supplied, or applies to be supplied, with electricity for its own consumption and not for the purposes of resupply to any other person.