



COMMERCE COMMISSION

Decision No. 425

Determination under the Electricity Industry Reform Act 1998 (“the EIR Act”), in the matter of an application for exemption of involvements in both an electricity lines business and an electricity supply business from the application of the EIR Act. The application is made by:

**NEWMARKET NEW ZEALAND LIMITED; and
AUCKLAND ONE LIMITED**

The Commission: Paula Rebstock

Commission Staff: D R Ainsworth

Summary of Application: Newmarket Newzealand Ltd and its subsidiary Auckland One Ltd seek an exemption under section 81 of the EIR Act, from the application of section 17 of the EIR Act.

Determination: The Commission, pursuant to section 81 of the EIR Act, exempts Newmarket Newzealand Ltd and Auckland One Ltd from the application of section 17 of the EIR Act in relation to a prohibited cross-involvement in an electricity lines and an electricity supply business. The exemption is subject to the conditions stated in this decision.

Date of Determination: 5 July 2001

Date of Exemption: On publication of the Notice of Exemption in the *New Zealand Gazette*.

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INTRODUCTION

- 1 On 21 March 2001 the Commerce Commission (“the Commission”) received an application from Newmarket Newzealand Ltd (NNL) and its subsidiary Auckland One Ltd (AOL) for exemption from the application of section 17 of the EIR Act.
- 2 The two companies sought an exemption from the application of section 17 of the EIR Act in respect of cross-involvements in electricity lines and electricity supply businesses. These cross-involvements arise as a result of the two companies’ ownership of electricity lines within commercial property in Auckland together with the sale of electricity to tenants of that property. Section 17 prohibits any person involved in an electricity lines business from being involved in an electricity supply business and vice versa. Those businesses are defined in sections 4 and 5 of the EIR Act
- 3 The Commission’s powers to exempt any 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 pursuant to section 81 of the EIR Act.

NEWMARKET NEWZEALAND LTD

- 4 NNL is a company incorporated in the British Virgin Islands and registered on the New Zealand overseas register of companies. It is the owner of a shopping mall in Papatoetoe, Auckland.
- 5 NNL has one property owning subsidiary, AOL. AOL owns four commercial properties in Newmarket, Auckland.

NNL AND AOL’S ELECTRICITY LINES BUSINESSES

- 6 NNL and AOL own and operate electricity lines in New Zealand, those lines being the electrical reticulation within the companies’ properties. NNL and AOL respectively convey [] and [] gigawatt-hours to tenants of their properties.

NNL AND AOL’S ELECTRICITY SUPPLY BUSINESSES

- 7 NNL sells [] gigawatt-hours of electricity to tenants in the shopping mall it owns in Papatoetoe, Auckland.
- 8 AOL sells [] gigawatt-hours of electricity to tenants of four commercial buildings it owns in Newmarket, Auckland.

INVOLVEMENTS

Electricity Lines Businesses

- 9 NNL and AOL are the owners of electricity lines in New Zealand. In terms of the EIR Act they both:
 - own a business that conveys electricity by line in New Zealand (s4(1)(a)); and
 - own and operate, directly or indirectly, lines in New Zealand and other core assets of an electricity lines business (s4(1)(b)).

10 Section 4(2)(a) of the EIR Act provides that:

4(2) None of the following activities brings a person within subsection (1):

(a) Conveying, together with its associates (if any), less than 2.5 GWh per annum:

Subsection (1) is the definition of an electricity lines business. Both NNL and AOL convey more than 2.5 gigawatt-hours per annum and do not fall within the section 4(2)(a) exclusion from the definition of electricity line business.

11 Both NNL and AOL are, therefore, electricity lines businesses in terms of the EIR Act.

12 NNL and AOL both:

- carry on an electricity lines business (s7(1)(a));
- exceed the 10% threshold in terms of control rights in that business (s7(1)(b)); and
- have material influence over that business (s7(1)(c)).

13 Therefore, both NNL and AOL are involved in an electricity lines business in terms of the EIR Act.

Electricity Supply Business

14 NNL and AOL, in terms of the EIR Act, sell electricity in New Zealand (s5(1)(a)(i)). Section 5(2)(a) of the EIR Act provides that:

5(2) None of the following activities brings a person within subsection (1):

(a) Selling or generating less than 2.5 GWh per annum:

Subsection (1) is the definition of an electricity supply business. Both NNL and AOL supply more than 2.5 gigawatt-hours per annum and do not fall within the section 5(2)(a) exclusion from the definition of electricity supply business.

15 Therefore, both NNL and AOL are electricity supply businesses in terms of the EIR Act.

16 NNL and AOL both:

- carry on an electricity supply business (s7(1)(a));
- exceed the 10% threshold in terms of control rights in that business (s7(1)(b)); and
- have material influence over that business (s7(1)(c)).

17 Therefore, both NNL and AOL are also involved in an electricity supply business in terms of the EIR Act.

PROHIBITED CROSS-INVOLVEMENT

18 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.”

- 19 NNL and AOL are involved, and wish to remain involved, in both an electricity lines and an electricity supply business. NNL and AOL have, in terms of section 17 of the EIR Act, a prohibited cross-involvement.
- 20 The two companies have, therefore, applied to the Commission for exemption from the application of the EIR Act and, in particular, from the requirement to comply with the ownership separation provisions of the EIR Act.

COMMISSION PROCEDURES

General

- 21 For the purpose of considering this application for exemption, the Commission, pursuant to 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 P R Rebstock.
- 22 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

- 23 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.3¹.
- 24 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 where 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.

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

¹ Practice Note No.3, September 1998, Electricity Industry Reform Act 1998 Commission’s Role and Processes.

(d) promoting effective competition in electricity generation and retail.”

25 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,⁽²⁾ expected.”

26 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)³ 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.”

EXAMINATION IN TERMS OF THE COMMISSION’S CRITERIA

Incentives or Opportunities to Inhibit Competition in the Electricity Industry

- 27 The Commission’s focus under this heading is on that part of the national electricity retail market comprising the electricity consumers who are tenants of NNL and AOL and whether an exemption would provide NNL and AOL with incentives or opportunities to inhibit competitive electricity supply to them.
- 28 The Commission considers that NNL and AOL could, in some circumstances, have the incentives and opportunities to inhibit competitive electricity supply to their tenants using the market power arising from their ownership of electricity lines.
- 29 However, the leasing of NNL and AOL’s properties occurs in a competitive property market.. The Commission considers that such competition for tenants partially mitigates against any incentive or opportunity for NNL and AOL to attempt to raise electricity prices by anti-competitive behaviour.
- 30 Further, if NNL and AOL attempt to raise the price they charge for electricity to above competitive levels, there is the potential for their tenants to obtain electricity from other

² For example, of the types provided for in section 19 of the EIR Act.

³ Defined using the same process as used for market definitions in respect of Commerce Act matters.

electricity retailers. Indeed a number of the two companies' tenants are already doing just that. The Commission will require as a condition to any exemption it grants that NNL and AOL shall not charge for the use of their electricity lines and shall permit access to those electricity lines by other electricity retailers. These conditions will mitigate the opportunities for NNL and AOL to act anti-competitively.

- 31 Therefore, given these two factors, the Commission considers that NNL and AOL's incentives and opportunities to inhibit competitive electricity supply to its lessees are no more than minimal and can be suitably dealt with by conditions attached to any exemption granted by the Commission.

Incentives or Opportunities to Cross-subsidise Generation Activities

- 32 Neither NNL or AOL are involved in electricity generation activities. This criterion is not relevant.

A Relationship Not at Arms Length

- 33 NNL and AOL propose to continue to own and operate both an electricity lines business and an electricity supply business. The two businesses will have common managers, premises and records. Managers will make decisions about both line and supply pricing and also about the terms for the granting of access to the two companies' lines by electricity retailers who wish to supply electricity their tenants. The relationship between the electricity lines and supply businesses will not be at arms length.
- 34 However the Commission considers that the potential effects of the relationship, not at arms length, can be tempered by the fact that neither NNL or AOL charges for the line function services they supply to their tenants.. NNL and AOL have undertaken that they will not introduce line charges for the use of their lines in the future. They are, in this respect, restricted in their ability to use the existence of a relationship not at arms length to defeat the purposes of the EIR Act. As a result, the Commission does not consider the potential effects of the relationship not being at arms length to be a material risk to the purposes of the EIR Act.

THE COMMISSION'S DECISION

- 35 Therefore, provided certain conditions are adhered to, the Commission considers that NNL and AOL's application satisfies the Commission's criteria for the granting of exemptions from the EIR Act.
- 36 The Commission exempts NNL and AOL from the application of section 17 of the EIR Act subject to the terms and conditions specified in the Notice of Exemption.
- 37 The Commission also notes that section 81(5) provides that the Commission may vary or revoke any exemption at any time.

NOTICE OF EXEMPTION

The Commission, pursuant to section 81 of the Electricity Industry Reform Act 1998, exempts Newmarket Newzealand Ltd and its subsidiary Auckland One Ltd from the application of section 17 of that Act in relation to prohibited cross-involvements in an electricity lines business and an electricity supply business.

The exemption is subject to the following terms and conditions:

- (a) That Newmarket Newzealand Ltd and Auckland One Ltd shall not introduce a charge to any consumer they supply with electricity, for the use of or related to, any electricity lines business that Newmarket Newzealand Ltd or Auckland One Ltd own or operate.
- (b) That Newmarket Newzealand Ltd and Auckland One Ltd shall not prevent the access to their electricity lines, on reasonable terms and within a reasonable time, that any electricity supply business may require to supply electricity to any consumer connected to such lines.
- (c) That Newmarket Newzealand Ltd and Auckland One Ltd shall not enforce any clause in any lease or other agreement with their tenants which requires a tenant to be supplied with electricity by Newmarket Newzealand Ltd or Auckland One Ltd, so that any tenant shall be free to choose that tenant's electricity supplier.
- (d) That Newmarket Newzealand Ltd and Auckland One Ltd will use their best endeavours to provide such reasonable information that any tenant taking a supply of electricity from Newmarket Newzealand Ltd or Auckland One Ltd may request to enable that tenant to assess competitive options available to it for the supply of electricity.
- (e) That Newmarket Newzealand Ltd and Auckland One Ltd do not generate electricity.

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 day of 2001

The Commission