



COMMERCE COMMISSION

Decision No. 483

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

Mr Samford Lee Maier (Junior)

The Commission:

P R Rebstock
Donal Curtin

**Summary of the
Application:**

As a director of Mighty River Power Limited, Mr Samford Maier is involved in that company, an electricity supply business. As a director of New Plymouth Equity Advisers Limited he is involved in Powerco Limited, an electricity lines business. He seeks exemption from the application of s 17 of the EIR Act, in order to remain involved in both kinds of business.

Determination:

The Commission, in terms of s 81 of the EIR Act, exempts Mr Maier from the application of s 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 December 2002

Date of Exemption:

The exemption takes effect from the date of the publication of a Notice of Exemption in the *New Zealand Gazette*.

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INTRODUCTION

- 1 On 2 September 2002, Mr Samford Lee Maier applied to the Commerce Commission (the Commission) for exemption from the application of s 17 of the EIR Act.
- 2 Mr Maier's involvements in electricity businesses arise from his directorships of Mighty River Power Limited (MRP) and New Plymouth Equity Advisers Limited (NPEAL).
- 3 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 s 81 of the EIR Act.

COMMISSION PROCEDURES

General

- 4 For the purpose of considering this application for exemption, the Commission, in terms of s 58 of the EIR Act which applies s 105 of the Commerce Act 1986 to the EIR Act, has delegated its powers under s 81 of the EIR Act to Paula Rebstock and Donal Curtin.
- 5 The Commission's decision is based on an investigation conducted by its staff and their subsequent advice to the Commission.
- 6 The Commission has considered the material provided by Mr Maier in support of his application and obtained through its own investigation.

Criteria Used by the Commission to Consider Exemption Applications

- 7 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.3.¹
- 8 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:

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

- (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.”

9 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.”

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

“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 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.”

PARTIES

Mighty River Power Limited

- 11 MRP 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.
- 12 As a generator its principal asset is a series of power stations on the Waikato River. The total capacity of its power stations is approximately 1,100 megawatts, about 13% of national generation capacity.

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

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

- 13 In addition, MRP is an electricity retailer competing in the national retail electricity market in various locations.
- 14 In terms of the EIR Act, MRP:
- sells electricity in New Zealand (s 5(1)(a)(i));
 - generates electricity in New Zealand (s 5(1)(a)(iii));
 - owns and operates directly generators in New Zealand (s 5(1)(b));
 - owns and operates directly core assets of an electricity retail business which include the benefit of contracts to sell electricity (s 5(1)(c)); and
 - does not fall within any of the exclusions listed in s 5(2) or 5(3).
- 15 Therefore, MRP is an electricity supply business in terms of the EIR Act.

New Plymouth Equity Advisers Limited

- 16 NPEAL is a wholly owned subsidiary of New Plymouth District Council (NPDC). NPEAL is a Local Authority Trading Enterprise under the provisions of the Local Government Act. It provides commercial and professional advice to NPDC regarding its various investments, including but not limited to NPDC's investments in Powerco Limited (Powerco), Apex Consultants Limited, Hobson Investments Limited, forestry and airport investments. NPDC owns 47.7% of the control rights and equity return rights in Powerco.
- 17 NPEAL, itself, is neither an electricity supply business nor an electricity lines business in terms of the EIR Act.

Powerco Limited

- 18 Powerco is a public company listed on the New Zealand Stock Exchange. Its electricity distribution networks provides line function services to about 157,000 electricity consumers in the Taranaki, Wanganui, Manawatu, and Wairarapa regions. The total amount of electricity currently distributed by Powerco is about 2,000 GWh per annum.
- 19 Powerco has recently announced plans to purchase some of the electricity networks owned by UnitedNetworks Limited.
- 20 The shareholders of Powerco are
- NPDC 47.7%
 - Taranaki Electricity Trust 16.8%
 - Powerco Community Trust 3.7%

- 17,000 small shareholders 31.8%

21 In terms of the EIR Act, Powerco:

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

22 Therefore, Powerco is an electricity lines business in terms of the EIR Act.

PROHIBITED CROSS-INVOLVEMENT

23 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.”

24 Further, the EIR Act provides:

- That a person who is a director of a body corporate is a “manager” of that company (s 3);
- a person is involved in an electricity business if the person exceeds the 10% threshold in s 8 in respect of that business or has material influence over the business (s 7(1)(b) and s 7(1)(c));
- a person exceeds the 10% threshold in respect of an electricity business if the person—
 - has more than 10% of the control rights in the business; or
 - has more than 10% of the equity return rights in the business; or
 - is one of 2 or more associates who, in aggregate, have more than 10% of the control rights in the business; or
 - is one of 2 or more associates who, in aggregate, have more than 10% of the equity return rights in the business.
- without limiting the ordinary meaning of the expression “material influence”, a person is deemed to have material influence over an electricity business if the person is one of 2 or more associates who, together, have material influence over the business (s 11(3));
- person A is an “associate” of person B (and vice versa) if person A is a body corporate, and person B is a director of a related body corporate of that body

corporate (within the meaning of s 5(7) of the Securities Amendment Act 1988 (“SSA”)(s 12(1)(a)(iii)).

THE RELATIONSHIP BETWEEN MR MAIER, NPEAL AND POWERCO

- 25 As noted, Mr Maier is a director of NPEAL. NPEAL provides advice to its owner, NPDC, about NPDC’s investment in Powerco.
- 26 Mr Maier has submitted that NPDC is involved in an electricity lines business by virtue of its ownership of 47.7% of the control rights and equity return rights in Powerco. The Commission agrees with this submission.
- 27 Mr Maier has submitted that he is not involved in Powerco, despite his directorship of NPEAL, because:
- he does not have a “material influence” over Powerco (s 11); and
 - he does not meet the “10% threshold” (s 7(b)) as there is no “aggregation” under s 8(c) and s 8(d) (Mr Maier submits that an “aggregation” would require him to personally hold at least some of the control rights or equity return rights in Powerco, which is not the case).
- 28 In support of the proposition that Mr Maier has no “material influence” over Powerco, he submits that:
- he is one of three directors on the NPEAL Board, with the other directors having been involved in NPDC’s investment in Powerco for a longer period than Mr Maier and having a greater knowledge of Powerco’s history. No one director is more dominant than the others and meetings of the NPEAL Board are also attended by legal and financial advisors;
 - advice from NPEAL does not go directly to NPDC but to the NPDC Equity Subcommittee (formerly the NPDC Energy Subcommittee);
 - NPDC is not required to follow the advice of NPEAL or the NPDC Equity Subcommittee and can, and does, take advice from other parties.
- 29 The Commission notes that:
- as a general rule it considers that a director is capable of having an influence on a board, irrespective of the composition of that board. For instance, when considering whether companies are associated in the context of s 47 of the Commerce Act, the Commission takes note of any overlapping directorates or the ability of one company to appoint a director to the other company;
 - specifically, with respect to Mr Maier’s role with NPEAL, Mr Maier has had wide experience in the governance of the electricity industry, so the Commission anticipates that this experience would give weight to Mr Maier’s view amongst the other NPEAL directors and the NPDC;

- Mr Maier and his fellow directors owe an equivalent fiduciary duty to NPEAL, it cannot be said that Mr Maier has less responsibility to NPEAL than his fellow directors;
 - the Commission accepts that NPEAL is not a decision maker with respect to Powerco. However, the sole purpose of NPEAL is to provide advice to NPDC on NPDC's investments. Accordingly, the advice of NPEAL is likely to be highly influential in the decisions made by NPDC on its investments; and
 - NPDC is the single largest shareholder in Powerco, with close to a controlling interest in Powerco, and as such is likely to be able to exert a material influence over Powerco.
- 30 The Commission considers that NPEAL's role is focussed on corporate governance issues, rather than on advising on or monitoring operational issues. This view is reinforced by a submission received from Stuart Bauld of PricewaterhouseCoopers. PricewaterhouseCoopers is the principal adviser to NPEAL and Mr Bauld regularly attends NPEAL directors meetings, he stated:
- “from my involvement in advising NPEAL and NPDC [I can confirm] that NPEAL has never to my knowledge been involved in the operational aspects of Powerco. The concern of NPEAL is entirely focussed on such matters as the relative performance of Powerco in comparison to other electricity lines companies and matters important to the council as shareholder votes, the election of directors and in particular dividend policy.”*
- 31 The Commission sought information about the advice provided by NPEAL to the NPDC Equity Subcommittee. The minutes of the NPEAL Board meetings over a four month period indicated that, with respect to Powerco, NPEAL advised on:
- the Council's potential participation in a Powerco Capital Bond issue;
 - prudential requirements with respect to NPDC's investment in Powerco;
 - recommendations for voting at the Powerco Annual General Meeting on items relating to constitutional amendments, the appointment of directors, and the remuneration of auditors.
- 32 The Commission was also informed that NPEAL's responsibility was to evaluate information received from PricewaterhouseCoopers relating to the monitoring of business efficiency compared to the relevant peer group, and to ensure that Powerco's performance in these matters is comparable to other lines companies. The purpose of such evaluation is to ensure that the NPDC's investment in Powerco is still an appropriate investment.

The Commission's view

Involved

- 33 MRP is an electricity supply business under the EIR Act. Mr Maier is a “manager” of an electricity supply business, as defined under s 3 of the EIR Act, as he is “director” of MRP. A “manager” of an electricity supply business is deemed to have a “material influence” over an electricity business under s 11 of the EIR Act. Accordingly, Mr Maier is “involved” in an electricity supply business (s 7 of the EIR Act).
- 34 The issue is whether Mr Maier is also “involved” in an electricity lines business (i.e. Powerco), as he is a director of NPEAL. NPEAL advises NPDC on its investment in Powerco (although we understand that advice is related to governance issues and not operational matters). Mr Maier is involved with Powerco if he:
- carries on that business, either alone or together with his associates and either on his own or another’s behalf (a person carries on a business if the person owns or operates any of the core assets comprising the business);
 - exceeds the 10% threshold in s 8 in respect of that business; or
 - has a material influence over the business.

10% Threshold

- 35 Mr Maier is “involved” in Powerco if he exceeds the 10% threshold in respect of Powerco (s 7). Under s 8, Mr Maier exceeds the 10% threshold if he:
- has more than 10% of the “control rights” in Powerco;
 - has more than 10% of the “equity return rights” in Powerco;
 - is one of 2 or more “associates” who in aggregate, have more than 10% of the control rights in Powerco; or
 - is one of 2 or more “associates” who, in aggregate, have more than 10% of the equity return rights in Powerco.
- 36 Mr Maier himself does not hold 10% of the control rights or equity return rights in Powerco (s 8).
- 37 NPDC holds 47.7% of the control rights and equity return rights in Powerco (s 7(1)(b)). So NPDC meets the 10% threshold.
- 38 Mr Maier is an “associate” of NPDC if NPDC is a body corporate, and Mr Maier is a director of a related body corporate (s 12(1)(a)(iii)). Section 37L(4) of the Local Government Act 1974 provides that every territorial authority shall be a body corporate, and a district council is a “territorial authority” under that Act. NPDC is therefore a body corporate.

- 39 Section 12(1)(a)(ii) provides that a related body corporate has the meaning in s 5(7) of the SAA. The SAA states that a body corporate is related to another body corporate if the other body corporate is its holding company or subsidiary within the meaning of s 5 and s 6 of the Companies Act 1993. NPEAL is a subsidiary of NPDC, so NPEAL and NPDC are related under the EIR Act. Mr Maier is a director of NPEAL, a related body corporate of NPDC. Mr Maier and NPDC are therefore “associates” under the EIR Act.
- 40 Mr Maier submits that s 8(c) and s 8(d), because of the words “in aggregate” require him to hold control rights and equity return rights. The *Concise Oxford Dictionary* states that “aggregate” means:

“collected into one body; collective, total; ...sum total; assemblage...”

“a collection of, or the total of, disparate elements constituted by the collection of many units into one body, “the aggregate” as a whole...”

- 41 *The Shorter Oxford Dictionary* defines “aggregate” as:

“to gather together into one whole; to mass...to add as a member...to amount in the aggregate to...”

- 42 Hence “in aggregate” simply requires the total percentage of the control rights or equity return rights to be taken into account. There is no requirement that Mr Maier himself hold shares, as this would defeat the purpose of the EIR Act.
- 43 If correct, Mr Maier would meet the requirements of s 8(c) or s 8(d) if he held one share but not if he held none. The focus is rather on whether the relevant parties are associates. Accordingly NPDC and Mr Maier in aggregate own more than 10% of the control rights or equity rights. On this basis Mr Maier meets the 10% threshold and is “involved” in Powerco.

Material Influence

- 44 Section 11 of the EIR Act sets out the meaning of the term “material influence”. It provides as follows:

“(1)Without limiting the ordinary meaning of the expression “material influence” the following people are deemed to have material influence over an electricity business...

(3) A person is deemed to have a material influence over an electricity business if the person is one of 2 or more associates who, together, have material influence over the business...”

- 45 Mr Maier submitted that he does not have a “material influence” over Powerco within the ordinary meaning of those words and that he does not fall within paragraphs (a) to (f) of s 11 of the EIR Act.

- 46 To have “material influence” over Powerco Mr Maier on his own would need to be in a position to affect and/or influence Powerco, including, among other things, the amendments to the company’s constitution, the appointment of directors and the dividend policy. These are matters of primary importance in the running of the company and NPEAL’s ability to advise on such matters indicates an ability to affect and/or influence Powerco. The evidence is that NPEAL does advise on governance issues relating to Powerco. Accordingly NPEAL has material influence over Powerco. The question is whether Mr Maier as one of three directors also has a material influence. As it happens it is not necessary to reach a final view on that point.
- 47 It is necessary to consider whether Mr Maier is deemed to have a material influence by reason of s 11(3). Mr Maier is deemed to have a material influence over Powerco if Mr Maier is one of 2 or more associates who, together, have material influence over the business. NPDC has a material influence over Powerco. As discussed above, Mr Maier and NPDC are “associates” as Mr Maier is a director of NPEAL, a related body corporate of NPDC. Mr Maier, his fellow directors, NPEAL and NPDC are associates who together have a material influence over Powerco. Hence Mr Maier is deemed to be involved in an electricity lines business.

Conclusion

- 48 Mr Maier is “involved” in an electricity lines business as he meets the “10% threshold” and he is deemed to have a “material influence” over Powerco under s 11 of the EIR Act.

CONCLUSION WITH RESPECT TO PROHIBITED CROSS INVOLVEMENT

- 49 Given that Mr Maier is involved, and wishes to remain involved, in both an electricity lines and electricity supply business, the Commission finds that he has, in terms of s 17 of the EIR Act, a prohibited cross involvement.
- 50 Mr Maier has, therefore, applied to the Commission for exemption from the application of the EIR Act and, in particular, from the requirement to comply with s 17 of the EIR Act.

RELEVANT MARKETS

- 51 The Commission considers the relevant markets are those parts of the electricity generation, retail and distribution markets in which MRP and Powerco are operating.⁴

EXAMINATION OF MR MAIER’S INVOLVEMENTS IN TERMS OF THE COMMISSION’S CRITERIA

- 52 The Commission has considered each of the criteria, set out above, to assess whether an exemption should be granted to Mr Maier. This analysis follows. First, however, the

⁴ Recent views of these markets are set out in Decisions 470 and 471.

Commission sets out the results of its investigations into the nature of the advice that NPEAL provides, as this is relevant to the consideration of the criteria.

Nature of the Advice Provided by NPEAL

53 The nature of the advice provided by NPEAL is governed by the agreement between NPDC and NPEAL. A copy of this agreement was provided to the Commission.

54 This agreement provides that

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55 These responsibilities point to NPEAL’s role being focused on governance issues, rather than advising on or monitoring operational issues. This view is reinforced by a submission received from Stuart Bauld of PricewaterhouseCoopers. PriceWaterhouseCoopers is the principal advisor to NPEAL and Mr Bauld regularly attends NPEAL directors meetings. He indicated that: [

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56 To further assess this issue, the Commission sought information about the advice provided by NPEAL to the NPDC Equity Subcommittee. The minutes of the NPEAL Board meetings over a four month period indicated that, with respect to Powerco, NPEAL advised on:

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57 The Commission was particularly interested in NPEAL’s responsibility to [], as this potentially would lead NPEAL to consider and

advise upon operational matters of Powerco. NPEAL's response to the Commission's inquiries was that NPEAL's responsibility was to [

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- 58 On the basis of this information, the Commission is satisfied that the role of NPEAL with respect to Powerco is solely to advise NPDC on governance matters. NPDC does not seek, and NPEAL does not provide, advice on Powerco operational matters. This finding is relevant to the Commission's assessment of the criteria below.

Incentives Or Opportunities of Mr Maier To Inhibit Competition in the Electricity Industry

- 59 In previous decisions, for example Decision 471, the Commission has found that electricity lines businesses are natural monopolies over their distribution areas. Therefore, if the involvement of Mr Maier in an electricity lines business and an electricity supply business were to inhibit competition, one would expect it to be in the electricity retail business. In terms of this investigation, the question is whether Mr Maier's involvement in Powerco provides him with incentives or opportunities to favour MRP in an electricity retail market.
- 60 MRP supplies customers, in competition with other electricity retailers, who are connected to Powerco networks. To do so, MRP enters into a use of system agreement with Powerco. The opportunity to inhibit competition in the retail market might arise if the use of system agreement between Powerco and MRP competitively advantaged MRP by favouring MRP over other retailers.
- 61 The applicant has informed the Commission that the use of system entered into between Powerco and MRP is substantially the same as the use of system agreement entered into between Powerco and other electricity retailers. On that basis there would not appear to be any current arrangement whereby Powerco favours MRP.
- 62 Mr Maier's opportunity to influence Powerco in the future is only through NPEAL. As already established, the sole focus of NPEAL's advice is on governance issues. Until now, this has not included any advice on operational matters such as the use of system agreements entered into with retailers. Provided there is no change to this arrangement, Mr Maier would not have the opportunity to inhibit competition.
- 63 Therefore, subject to there not being any change in the focus of NPEAL's monitoring of Powerco and advice to NPDC, the Commission concludes that Mr Maier's involvement with Powerco and MRP does not create the incentive or opportunity to inhibit competition in the electricity retail markets.

Incentives or Opportunities of Powerco to Cross-subsidise MRP's Generation Activities From Powerco's Line Business

- 64 The mechanism by which Powerco's electricity lines business could potentially be used to subsidise MRP's generation activities, would be a use-of-system agreement negotiated between Powerco and MRP, which did not provide a proper commercial return to Powerco.

65 However, the relationship between NPEAL and Powerco, in particular the focus on governance rather than operational issues, means that the Commission does not see that the negotiation of such an agreement could be influenced by the presence of Mr Maier as a director of NPEAL and MRP, provided there is no change to this arrangement. Therefore, subject to there not being any change in the focus of NPEAL's monitoring of Powerco and advice to NPDC, the Commission does not consider Mr Maier's involvement in Powerco and MRP creates incentives or opportunities for Powerco to cross-subsidise MRP's generation activity.

A Relationship between MRP and Powerco Not at Arms Length due to Mr Maier's Influence

66 Mr Maier proposes to continue to be a director of both MRP and NPEAL. As such, given his material influence on each, there will be a relationship between an electricity supply business and an electricity lines business which will not be at arms length.

67 However, because the focus of NPEAL with respect to Powerco is solely on governance matters rather than operational matters, the Commission considers that Mr Maier does not have the opportunity to influence this relationship in any way that is more than minimal. As a result, in this case, 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.

NOTICE OF EXEMPTION

The Commission, pursuant to s 81, exempts Mr Samford Lee Maier (Junior) from the application of s 17 of the Electricity Industry Reform Act 1998 (EIR Act) 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) Mr Maier shall exclude himself, on the basis of a legal conflict of interest, from any discussion about, or consideration of, advice by NPEAL concerning any relationship or transactions which Powerco has or proposes to have with any electricity retailer or generator.
- (b) After one year from the date of this exemption, NPEAL shall provide the Commerce Commission with copies of all advice it has provided that relates to Powerco.

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

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

Dated this 17th day of December 2002

Paula Rebstock
Deputy Chair