



COMMERCE COMMISSION

Decision No. 358

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

COLWALL PROPERTY INVESTMENT LIMITED

The Commission: K M Brown
E C A Harrison
E M Coutts
P R Rebstock

Commission Staff: A Mladenovic

Summary of Application: Colwall Property Investment Limited, which is involved in an electricity lines business and electricity supply business, seeks an exemption, pursuant to section 81 of the EIR Act, from the application to it of the EIR Act in order to remain involved in both kinds of business.

Determination: The Commission, pursuant to section 81 of the EIR Act, exempts Colwall Property Investment Limited from the application of section 17 of the EIR Act in relation to the conveyance and supply of electricity to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre. The exemption is subject to the terms and conditions stated in this Decision.

Date of Determination: 2 June 1999.

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

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INTRODUCTION

- 1 The Commerce Commission (the Commission) received on 3 May 1999 an application from Colwall Property Investment Limited (Colwall) seeking an exemption under section 81 of the Electricity Industry Reform Act 1998 (the EIR Act) in respect of Colwall.
- 2 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 section 81 of the EIR Act.

COLWALL PROPERTY INVESTMENT LIMITED

- 3 Colwall is a privately owned company registered in New Zealand. It is a wholly owned subsidiary of Perfect Match Investment Limited, a company registered in Hong Kong. Colwall owns the property in the Auckland Central Business District situated at 120 Albert Street. The property incorporates four distinct operations: a commercial office tower known as WestpacTrust Tower; a retail shopping centre known as the Atrium on Elliott Shopping Centre; the Centra Auckland Hotel, a 332 room hotel; and a carpark building known as the Atrium Carpark.
- 4 Colwall leases WestpacTrust Tower and Atrium on Elliott Shopping Centre to approximately 70 lessees who either lease commercial offices or operate retail businesses. Managers appointed by Colwall operate the Centra Auckland Hotel and Atrium Carpark on behalf of Colwall.
- 5 Colwall has no subsidiaries. It does, however, have two associated companies operating in New Zealand. They are Chalon Investments Limited, which owns the vacant site adjacent to the property at 120 Albert Street owned by Colwall, and Winstone Pulp International Limited, which has interests in forestry and a pulp mill in the central North Island.

Supply of Electricity by Colwall

- 6 Colwall currently purchases approximately [] GWh of electricity per annum. This electricity is consumed by Colwall as to approximately [] GWh in respect of the Centra Auckland Hotel and Atrium Carpark and for the provision of common building services as to approximately [] GWh. The balance of approximately [] GWh is supplied by Colwall directly to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre. The objective behind the bulk purchase and supply of electricity by Colwall is to achieve a better, more cost effective electricity supply deal than would otherwise be achieved by Colwall and each of Colwall's tenants acting independently to arrange their supply of electricity.
- 7 The cost of electricity utilised in providing common building services to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre (eg, air condition systems, elevators, shared lobby areas), along with the costs of general building running expenditure such as cleaning and property insurance premiums, is recovered by Colwall

through charging the tenants operating expenses allocated on the basis of each tenant's floor space occupation.

- 8 Electricity directly consumed by tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre is sold to them by Colwall in accordance with the lease agreements in respect of those tenants. The electricity is charged by Colwall on the basis of actual consumption measured by separate meters dedicated to the floor space occupied by each tenant.
- 9 Colwall does not generate electricity.

Embedded Electrical Wiring Systems

- 10 Electricity supplied to Colwall, including for direct consumption by Colwall's tenants, is conveyed by means of the existing embedded electrical wiring systems within the buildings situated at Colwall's property at 120 Albert Street. The embedded electrical wiring systems are the only electricity distribution systems owned or operated by Colwall.

THE EXEMPTION APPLICATION

- 11 Pursuant to section 81 of the EIR Act, Colwall seeks:

- an exemption from the application of section 17 of the EIR Act; and
- a short term exemption from the application of sections 24 and 25 of the EIR Act for a period of three months after the Commission's decision in relation to an exemption from the application of section 17 of the EIR Act, in the event that the Commission's decision is to decline to grant an exemption in respect of section 17.

COMMISSION PROCEDURES

- 12 For the purpose of considering Colwall's application for an exemption under section 81 of the EIR Act, 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 K M Brown, E C A Harrison, E M Coutts and P R Rebstock.
- 13 The Commission's decision is based on an investigation conducted by its staff and their subsequent advice to the Commission.

INVOLVEMENTS AND CROSS-OWNERSHIP PROHIBITION

- 14 Section 17 of the EIR Act provides:

“17. Cross-ownership Prohibition – (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.”

- 15 Accordingly, it is first necessary to consider in relation to Colwall's application whether Colwall is *involved* (as defined in section 7 of the EIR Act) in an *electricity lines business* and *electricity supply business* (as those terms are defined in the EIR Act).

Electricity Lines Business

- 16 In Decision 351A¹, the Commission considered the application of the EIR Act to a property company, Trans Tasman Properties Limited (TTP). The broad facts underlying Colwall's application to the Commission are similar to those considered by the Commission in Decision 351A. TTP owns the existing embedded electrical wiring systems within the Finance Centre² (and its other buildings) and purchases electricity to sell to tenants of the Finance Centre in accordance with lease agreements. In addition, TTP purchases electricity which it utilises in providing common building services to tenants of the Finance Centre.
- 17 The Commission concluded in Decision 351A that ownership of the embedded electrical wiring systems within buildings constituted an involvement in an electricity lines business in terms of the EIR Act. The Commission sees no reason to alter this view in relation to the embedded electrical wiring systems within Colwall's buildings.
- 18 Accordingly, the Commission concludes that Colwall is involved in an electricity lines business in terms of the EIR Act. Colwall:

- owns a business that conveys electricity by line in New Zealand (section 4(1)(a));
- owns and operates, directly, lines in New Zealand and other core assets of an electricity lines business (section 4(1)(b));
- has no activities exempted by section 4(2);
- carries on an electricity lines business alone or together with associates (section 7(1)(a));
- exceeds the 10% threshold in terms of control and equity return rights in that business (section 7(1)(b)); and
- has material influence over that business (section 7(1)(c)).

Electricity Supply Business

- 19 As noted earlier, Colwall currently purchases electricity for the following purposes:
- for its own consumption in relation to the Centra Auckland Hotel and Atrium Carpark;
 - for the provision of common building services; and

¹ Decision No. 351A, *Trans Tasman Properties Ltd*, Commerce Commission, 6 May 1999.

² The Finance Centre is a group of four adjacent properties situated in the Auckland Central Business District, providing commercial office space.

- for selling to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre for their direct consumption.
- 20 In respect of electricity purchased for its own consumption, Colwall clearly could not be considered an electricity supply business in terms of the EIR Act. Section 5(2)(b) of the EIR Act excludes the generation or sale of electricity by a person solely for its own consumption or for the consumption of its associates from the term *electricity supply business*.
- 21 The supply of electricity by Colwall for the purpose of providing common building services does not constitute, in the Commission's view, an electricity supply business in terms of the EIR Act. In this respect, the Commission stated in Decision 351³, at paragraph 11:
- “The purchase of such electricity by TTP is to enable it to provide and maintain rental properties to a standard required by tenants, rather than for the purpose of direct consumption by tenants. The electricity is consumed by assets owned by, and not leased from, TTP. The recovery of the cost of this electricity by TTP does not, in the Commission's view, represent selling electricity but is instead the recovery of the costs of various services provided by TTP which are integral to managing and operating its rental properties, and for which, in some instances, electricity is a necessary input.”
- 22 In respect of the sale of electricity by Colwall to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre for their direct consumption, the Commission considers, consistent with Decision 351A in relation to TTP's Finance Centre, that Colwall is *involved* (as defined in section 7 of the EIR Act) in an electricity supply business in terms of the EIR Act. Colwall:
- sells electricity in New Zealand (section 5(1)(a)(i));
 - is not exempted from section 5(1) because it sells greater than 2.5 GWh per annum of electricity to tenants (section 5(2)(a));
 - carries on an electricity supply business alone or together with associates (section 7(1)(a));
 - exceeds the 10% threshold in terms of control rights and equity return rights in that business (section 7(1)(b)); and
 - has material influence over that business (section 7(1)(c)).
- 23 Accordingly, the Commission concludes that Colwall is cross-involved in terms of section 17 of the EIR Act in relation to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre.

CRITERIA USED BY THE COMMISSION FOR EXEMPTION APPLICATIONS

- 24 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 has set out its role and processes in Practice Note No. 3⁴.

³ Decision No. 351, *Trans Tasman Properties Ltd*, Commerce Commission, 1 April 1999.

⁴ Practice Note No. 3, *Electricity Industry Reform Act 1998 Commission's Role and Processes*, September 1998.

25 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 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
- (d) promoting effective competition in electricity generation and retail.”

26 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,⁵ expected.”

27 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 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)⁶ within the electricity industry;
- The nature of any incentives or opportunities created;

⁵ For example, of the types provided for in section 19 of the EIR Act.

⁶ Defined using the same process as used for market definitions in respect of Commerce Act matters.

- 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.”

RELEVANT MARKET

28 In terms of the Commission’s criteria set down in Practice Note No. 3, the national electricity retail market is relevant to the facts of Colwall’s application for an exemption under section 81 of the EIR Act.⁷

EXAMINATION IN TERMS OF THE COMMISSION’S CRITERIA

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?
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- 29 The Commission has concluded in respect of the sale of electricity by Colwall to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre that Colwall is both an electricity lines business and electricity supply business in terms of the EIR Act. Colwall is therefore cross-involved in terms of section 17 of the EIR Act. The question to consider is whether allowing Colwall’s involvements in both businesses creates incentives or opportunities to inhibit competition in the electricity industry.
- 30 Colwall has argued to the Commission that by not granting it an exemption from section 17 of the EIR Act, competition for electricity supply will be reduced (and its tenants made worse off) because most tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre would be left to purchase their electricity either directly from their incumbent retailer or an alternative bulk supplier. Colwall would choose to remain only an electricity lines business in terms of the EIR Act if it was refused an exemption. Colwall further argues that a tenant purchasing their electricity directly from the incumbent retailer would be unable to reap the benefits of a bulk electricity supply deal through collective buying power. In addition, an alternative bulk supplier would charge more than Colwall because (unlike Colwall) the alternative supplier would not have an objective to maximise Colwall’s occupancy rate by ensuring that the tenants’ total occupation costs, including the cost of electricity, are minimised.
- 31 Part of the recent electricity sector reform through the EIR Act has included the requirement to separate electricity distribution functions (lines) and electricity retailing and generation functions (supply) in order to enhance competition and choice in respect of supply. The EIR Act recognises that the market power of an electricity lines business enables the use of various mechanisms to inhibit competition in electricity retailing. Such mechanisms include:

⁷ Other markets in the electricity industry, for example the wholesale electricity market, the electrical construction and maintenance market, the market for the reticulation of new subdivisions, the local distribution market, and the national electricity generation market, do not appear to be relevant to this application for exemption.

- charges to electricity retailers for access to lines and contract administration charges over and above line charges;
 - cross-subsidies from line charges to electricity retail charges;
 - delays in permitting electricity retailers to have access to lines through use-of-system contractual arrangements.
- 32 Competition and choice in respect of the supply of electricity to Colwall's tenants should present the tenants with an opportunity to minimise their electricity costs. Colwall's involvements in an electricity lines business and electricity supply business in terms of the EIR Act provide Colwall with incentives and opportunities to inhibit competition in the supply of electricity to its tenants by, for example, imposing unreasonable line charges and access terms in respect of the embedded electrical wiring systems within WestpacTrust Tower and Atrium on Elliott Shopping Centre, or cross-subsidising electricity sales from line charges. Colwall's incentive is that it benefits not only from selling electricity to tenants but also by being part of a bulk electricity supply deal for its own consumption, thus reducing its operating costs.
- 33 In Colwall's case it is significant that Colwall does not internally account for its embedded electrical wiring systems in WestpacTrust Tower and Atrium on Elliott Shopping Centre or impose any line charges for the conveyance of electricity across those systems. If Colwall is required to provide the services of its electricity lines business (ie, the embedded electrical wiring systems) at no cost to its tenants, any incentives or opportunities to defeat the purposes of the EIR Act would be significantly restricted.
- 34 Colwall also does not require use-of-systems agreements for the embedded electrical wiring systems for tenants to be supplied electricity directly by an electricity retailer rather than by Colwall. If Colwall decided in the future to require use-of-system agreements and then attempted to prevent an electricity retailer from supplying electricity directly to Colwall's tenants by, for example, refusing to enter into or delaying a use-of-system agreement, Colwall would be at risk under both the Commerce Act 1986 and the EIR Act. Colwall must act within the requirements of both the Commerce Act and EIR Act to enable its tenants to switch to an electricity retailer if they so choose. This would include the provision by Colwall to all tenants of relevant electricity usage and billing information on a timely basis to enable the tenants to solicit competing bids for electricity supply.
- 35 The Commission considers that, given continued provision of line services at no charge, reasonable access by other electricity suppliers to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre, and the provision by Colwall to all tenants of relevant electricity usage and billing information on a timely basis, the granting of an exemption from the application of the EIR Act, and in particular from the requirement to comply with the ownership separation provisions, will not provide Colwall with incentives or opportunities to inhibit competition in the national electricity retail market.

Incentives or Opportunities to Cross-subsidise Generation 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 activities from electricity lines businesses?

- 36 Colwall is not involved in electricity generation. Accordingly, this criterion is not relevant to the Commission's analysis.

A Relationship Not at Arms Length

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?

- 37 Colwall proposes 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 Colwall's embedded electrical wiring systems by electricity retailers who wish to compete with Colwall's electricity supply business. The relationship between Colwall's electricity lines and supply businesses will not be at arms length if Colwall is permitted to continue both businesses.
- 38 However, the Commission considers that the potential effects of the relationship not being at arms length can be tempered by the fact that Colwall supplies line services to its tenants, to whom it also supplies electricity, at no charge. Colwall would be restricted in its ability to use the existence of a relationship not at arms length to defeat the purposes of the EIR Act by being bound to continue to provide line services at no charge. 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

- 39 Colwall's application to the Commission under section 81 of the EIR Act for an exemption from the application of section 17 of the EIR Act passes two of the three criteria used by the Commission to decide upon exemptions from the Act, given continued provision by Colwall of line services at no charge, reasonable access to Colwall's embedded electrical wiring systems by other electricity suppliers to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre, and the provision by Colwall to all tenants of relevant electricity usage and billing information on a timely basis. The third criterion is not applicable.
- 40 Accordingly, the Commission exempts Colwall from the application of section 17 of the EIR Act in relation to the conveyance and supply of electricity to tenants of

WestpacTrust Tower and Atrium on Elliott Shopping Centre, subject to the terms and conditions specified in the Notice of Exemption.

- 41 In making its decision the Commission notes that the facts revealed in Colwall's application are particular to its situation alone. The Commission also notes that section 81(5) provides that the Commission may vary or revoke any exemption at any time.
- 42 Given the Commission's decision, there is no need for the Commission to consider a short term exemption for Colwall from the application of sections 24 and 25 of the EIR Act.

NOTICE OF EXEMPTION

The Commission, pursuant to section 81 of the Electricity Industry Reform Act 1998 (the EIR Act), exempts Colwall Property Investment Limited from the application of section 17 of the EIR Act in relation to the conveyance and supply of electricity to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre.

The exemption is subject to the following terms and conditions:

- (a) That Colwall Property Investment Limited does not introduce a charge to any person for the use of, or in connection with, its electricity lines business in relation to the supply of electricity to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre.
- (b) That Colwall Property Investment Limited does not prevent access, on reasonable terms and on a timely basis, to any embedded electrical wiring systems it owns in relation to WestpacTrust Tower and Atrium on Elliott Shopping Centre, by any electricity supply business wanting to supply electricity to tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre.
- (c) That Colwall Property Investment Limited provides all tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre to whom it supplies electricity with relevant electricity consumption and billing information, on a timely basis, to enable the tenants to assess competitive options for the supply of their electricity.
- (d) That if Colwall Property Investment Limited enters into any new, or materially changes its current, contracts, arrangements, or understandings with tenants of WestpacTrust Tower and Atrium on Elliott Shopping Centre or their assigns in relation to the conveyance or supply of electricity, Colwall Property Investment Limited notifies the Commission.

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

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

Dated this 2nd day of June 1999

The Commission