



21 March 2012

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**Application for Exemption from Part 3 of Electricity Industry Act 2010 under section 90 on behalf of Mr James Miller, Proposed Director of Mighty River Power Limited**

#### APPLICATION

1. Under section 90 of the Electricity Industry Act 2010 (the Act), application is hereby made to the Electricity Authority (the Authority) for an exemption from the application of sections 75, 77-79 and 88 of Part 3 of the Act. The date of the application is the date of this letter.

#### DETAILS OF THE PERSON FILING THE APPLICATION

2. This application is jointly made by Mr James Miller and Mighty River Power Limited.
3. Please direct any correspondence or queries about the application to James Craig (Partner) and Alicia Murray (Senior Associate) at Simpson Grierson in the first instance. Our contact details are:

Simpson Grierson  
88 Shortland Street  
Auckland,

James Craig - DDI 09 977 5125, and email [james.craig@simpsongrierson.com](mailto:james.craig@simpsongrierson.com)

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#### CONFIDENTIALITY

4. The fact and content of this application are not confidential. However we request that the Authority treat as confidential and commercially sensitive the names of Mighty River Power's (through Mercury Energy) customers on AIAL's network which are **attached** as a schedule to this application. This schedule should not be made publicly available by the Authority without first consulting with us.

#### TIMETABLE

5. Following the announcement on 20 March 2012 of Mr Miller's proposed appointment as a director of Mighty River Power by the Minister for State-owned Enterprises (Hon. Tony Ryall), Mighty River Power intends to appoint Mr Miller to its Board of Directors

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no later than 1 May 2012. Accordingly, we would be grateful if the Authority could provide its final decision on this application as soon as possible, and in any event by no later than **Friday 20 April 2012**. If for any reason the Authority will have problems in reaching a decision in this timeframe, we would be grateful if you could let us know as early as possible. We can provide further information about the reasons for urgency if that would assist.

#### **BACKGROUND TO APPLICATION**

6. Mr Miller is currently, and will continue to be, a director of Auckland International Airport Limited (AIAL). Mighty River Power wishes to appoint Mr Miller to its Board of Directors.
7. We note that Mr Miller is also currently a director of Vector Limited, but that he will be resigning as a director of Vector before his appointment to the Board of Mighty River Power becomes effective. As a result, Mr Miller's directorship of Vector will not be relevant for the purposes of Part 3 of the Act.

#### **AIAL's Business**

8. AIAL owns and operates Auckland Airport, the principal gateway for more than 70% of visitors to this country. AIAL delivers the infrastructure and services to support and facilitate business and leisure aircraft travel services, and acts as a facilitator of the movement of freight for both export and import industries. In addition to its aeronautical business, it provides a wide variety of retail, commercial and customer services.
9. AIAL was listed on the New Zealand Stock Exchange in July 1998 and on the Australian Stock Exchange in February 1999. Its two largest shareholders are Auckland Council Investments Limited and New Zealand Superannuation Fund Nominees Limited.
10. AIAL owns the electricity distribution network at the airport. The network operates at 11,000 and 400 volts and comprises transformers, switchgear and underground cables. The network connects to Vector Limited's citywide network at the perimeter of the airport.
11. AIAL distributes electricity to 376 consumers at the airport. Of the 102 GWh per annum distributed over AIAL's network, 31.2 GWh is for AIAL's own use. Because AIAL distributes 102 GWh over its network, it is over the 5GWh threshold for a distributor under clause 2(c) of Schedule 2 of the Act.
12. Electricity retailers TrustPower, Genesis Power Limited, Contact Energy Limited, Meridian Energy Limited, Simply Energy and Mercury Energy (Mighty River Power) each have access to AIAL's network in accordance with standardised Use of System Agreements in order that they may retail electricity to consumers connected to AIAL's network.
13. The existing directors of AIAL are John Brabazon, Richard Didsbury, Brett Godfrey, James Miller, Keith Turner, Henry van der Heyden and Joan Withers.

#### **Mighty River Power's Business**

14. As the Authority is aware, Mighty River Power is an electricity generator and retailer. It was formed as a result of the division of the Electricity Corporation of New Zealand into three separate companies in April 1999 and is a State-Owned Enterprise.

15. It owns nine hydro-electric power stations on the Waikato River, a gas co-generation plant at Southdown in Auckland and a (non-operative) thermal plant at Marsden. In addition, it jointly owns geothermal power stations at Mokai and Nga Awa Purua, and is the sole owner of geothermal power stations at Rotokawa and Kawerau.
16. Mercury Energy, Mighty River Power's electricity and gas retail division, competes in the national retail electricity market in various locations.
17. Mercury Energy also supplies electricity to various consumers on the AIAL distribution network (as set out in the Schedule attached to this application; referred to as the "**Mighty River Power Airport Customers**"). Mercury Energy does not supply electricity to AIAL itself. (We have generally referred in this application to Mighty River Power, with such references intended to include Mercury Energy where applicable.)
18. The existing directors of Mighty River Power are Michael Allen, Prudence Flacks, Jonathan Hartley, Trevor Janes, Sandy Maier, Joanne McLean, Tania Simpson, Keith Smith and Joan Withers (Chair). Mr Maier is standing down as a director, and Mighty River Power intends to appoint Mr Miller to replace him.

#### **DETAILS OF THE EXEMPTION SOUGHT**

##### **Particular Sections of Part 3 in respect of which an exemption is sought**

19. Mr Miller and Mighty River Power seek an exemption from the application of the following sections of the Act:
  - (a) Section 75, which prohibits a person who is involved in a distributor from being involved in a generator;
  - (b) Section 77, under which a director of a distributor, where there is a connected retailer, is obliged to ensure that the distribution business has a comprehensive written use-of-systems agreement, and that the terms of that agreement meet certain requirements;
  - (c) Section 78, under which a director of the distributor must not pay, or offer to pay, any consideration to a retailer in respect of the transfer to a connected retailer of any retail customers who are connected to the distributor's networks;
  - (d) Section 79, under which a director of a distributor must ensure that any rebates or dividends do not discriminate between customers of a connected retailer and customers of other retailers; and
  - (e) Section 88 which requires each director of a distributor referred to in section 77(1) to ensure that the director discloses the quantity of electricity sold each financial year by connected retailers to customers who are connected to its local network.
20. As far as we are aware, no applications for exemption from Part 3 of the Act have been submitted to the Authority since the Act came into force on 1 November 2010.
21. However, exemptions to section 17 of the Electricity Industry Reform Act 1998, similar in nature to the exemption the applicants are seeking, have been granted in the past by

the Commerce Commission. In particular, we rely on the following exemptions granted by the Commerce Commission:

- (a) Decision 676 dated 31 July 2009 which related to the appointment of Joan Withers, a director of AIAL, to the Board of Mighty River Power;
- (b) Decision 649 dated August 2008 which related to the appointment of Stephen Reindler, a director of AIAL, to the Board of Meridian Energy;
- (c) Decision 629 dated 19 November 2007 which related to the appointment of Lloyd Morrison, a director of TrustPower Limited (which generates and retails electricity) and Wellington International Airport Limited (which conveys and sells electricity), to the Board of AIAL; and
- (d) Decision 384 dated March 2000 which related to the appointment of Joan Withers to sit on the Boards of both Meridian Energy and AIAL.

22. These exemptions were granted with conditions. We propose that the same conditions applied to Ms Withers in Decision 676 be applied to Mr Miller in the present application. These conditions are as follows:

- (a) While Mr Miller is a director of both AIAL and Mighty River Power, Mr Miller will not participate in any discussions or decision making by Mighty River Power and/or AIAL regarding matters that relate to or could affect or favour the supply of electricity by Mighty River Power (or disadvantage any other business selling electricity on AIAL's network other than Mighty River Power) on AIAL's electricity distribution network or the provision of electricity lines services by AIAL to Mighty River Power, including:

- (i) the selection of, and any negotiation with, any electricity retailer for the supply, or intended supply, of electricity to AIAL; and
- (ii) the supply, or intended supply, of electricity by Mighty River Power to any new, or existing, consumers on AIAL's electricity distribution network;

and shall not disclose the outcomes of any discussions or decision making by AIAL to Mighty River Power (and vice versa) on those matters;

- (b) Mr Miller will confirm to the Authority, in writing, that the cross-involvement to which this exemption applies has ceased within one calendar month of the cross-involvement ceasing to exist;
- (c) This exemption will expire when the Authority publishes on its website Mr Miller's written confirmation that his cross-involvement has ceased; and
- (d) The exemption is specific to the cross-involvements created through Mr Miller's involvement in AIAL and Mighty River Power. It does not extend to any other interest or future cross-involvement of Mr Miller.

#### **The nature of the involvement of Mr Miller under Part 3 of the Act**

23. Section 74 of the Act states that a person is "involved" in a distributor, a generator or a retailer if the person:

*"... (c) has material influence over a business that does any of those things [distribution, generation or retail]."*

24. "Material influence" is defined in clause 7 of Schedule 2 of the Act, which provides:
- "(1) Without limiting the ordinary meaning of the expression **material influence**, the following people are deemed to have material influence over a business:*
- (a) a director ... of a person that carries on the business"*
25. Therefore, Mr Miller would be involved in a distributor (AIAL) and involved in a generator (Mighty River Power) through his proposed directorships of both companies.
26. Under section 75, a person who is involved in a distributor must not be involved in a generator that has a total capacity of more than 250MW that is generated by one or more generating plants that are directly connected to the national grid.
27. Mighty River Power's generation assets include various hydro power stations, geothermal stations and a gas-fired generation plant, producing a total of 1601MW. This generation is directly connected to the national grid. As a result, section 75 will apply.
28. Sections 77-79 apply where there is a connected retailer. Under s77(3) "connected retailer" means *"a retailer –*
- (a) That is involved in retailing more than 5 GWh of electricity on the distributor's local network in a financial year to customers who are connected to that network; and*
- (b) In respect of which the distributor, or any person involved in the distributor, is involved."*
29. Mighty River Power, through Mercury Energy (its retail and gas division), retails more than 5GWh of electricity to customers connected to AIAL's distribution network.
30. For the sake of completeness, we note:
- (a) section 76 does not apply since Mighty River Power does not have 50MW of generation connected to AIAL's network (ie it is not a "connected generator"), and it does not retail more than 75GWh of electricity to customers who are connected to AIAL's network (ie it is not a "connected retailer" for the purposes of that section;
- (b) accordingly the arm's length rules in Schedule 3 of the Act do not apply (since clause 1(1) provides they relate back to section 76). This in turn means section 89 does not apply;
- (c) Mighty River Power is not a "connected generator" for the purposes of sections 77-79 since it does not have generation connected to AIAL's network.

### **The relevant markets in the electricity industry**

31. Consistent with the previous analogous Commerce Commission decisions referred to above, the relevant markets for the purposes of this application are the national electricity generation and wholesaling market, the electricity retailing markets and the

local electricity distribution market that corresponds with AIAL's electricity distribution network.

### **The nature of any incentives or opportunities created**

#### *National Electricity Generation and Wholesaling Market*

32. Mighty River Power's generation assets are not directly connected to AIAL's distribution network, nor is it intended that they will be in the future. The applicants therefore consider that the granting of the exemption sought would not create incentives or opportunities to inhibit competition in the national electricity generation or wholesaling markets.

#### *Electricity Retailing Markets*

33. Consistent with the Commission's approach to Decisions 676, 649 and 629, the applicants submit that the focus of the Authority's enquiry in relation to electricity retailing markets should be on AIAL's distribution network (i.e. the retail electricity market comprising the Mighty River Power Airport Customers connected to AIAL's network at Auckland International Airport).
34. As the Commission found in Decisions 676, 649 and 629, the opportunities for competition to be affected that are created by Mr Miller's appointment to the Mighty River Power Board can be effectively addressed by limitations on his participation in matters that relate directly to electricity supply or electricity lines services between Mighty River Power and AIAL. Effective limitations can be achieved by the combination of:
- (a) Clause 7.10 of the Mighty River Power Board Charter which provides that a director who is interested in a transaction entered into, or to be entered into, by the company "*may not (except in relation to indemnities and insurance for directors and employees or with the Shareholders' consent) vote on a matter relating to the transaction*". (Clause 26.1.1 of Mighty River Power's Constitution makes the same point.) Amongst other things, this would remove for instance any risk of opportunities for competition in relation to the supply of electricity to the Mighty River Power Airport Customers to be inhibited by Mr Miller exercising his vote as a Mighty River Power director;
  - (b) The imposition of the proposed conditions of exemption on the terms set out above in para. 22. In particular Mr Miller would be prohibited from participating in discussions about the terms and conditions of (and ongoing administration of) the use of system agreement between Mighty River Power/Mercury and AIAL. Therefore there will be no incentives or opportunities for Mr Miller to inhibit competition in AIAL's electricity retail market by favouring Mighty River Power relative to other retailers in relation to use of system agreement matters. In any event, Mighty River Power supplies electricity only to AIAL's tenants and not to AIAL itself, and it is only one of a number of electricity retailers that do so, with the result that Mighty River Power's ability to limit competition in this market is limited;
  - (c) Lastly, to the extent that Mr Miller, in his capacity as a director of Mighty River Power, has opportunities or incentives to inhibit competition by means other than by the formal voting process, these opportunities can be effectively addressed by the proposed condition above prohibiting Mr Miller from participating in any discussions or decision making by Mighty River Power regarding matters relating to the supply of electricity to the Mighty River

Power Airport Customers. This would apply to discussions and decision making at both the board level and the management level.

*Regional electricity distribution markets*

35. The regional electricity distribution market that is relevant to this application is the electricity distribution market that corresponds with AIAL's distribution network (as noted by the Commission for instance in Decision 629).
36. Since AIAL's network is a local natural monopoly, the granting of this exemption would not affect the level of existing competition or the scope for potential competition within this market. Therefore, the applicants submit that the granting of an exemption would not create incentives or opportunities to inhibit competition in this market.

**Would the exemption promote, or not inhibit, competition in the electricity industry?**

37. For the reasons set out above, and subject to the conditions of exemption proposed, the applicants submit that the exemption will not inhibit competition in the electricity industry.

**Would the exemption permit any involvement in a distributor and a generator or a retailer that may create incentives or opportunities to inhibit competition in the electricity industry?**

38. For the reasons set out above, and subject to the conditions of exemption proposed, the applicants submit that the exemption will not create any incentives or opportunities to inhibit competition in the electricity industry.

**Would the exemption, in respect of an involvement, create incentives or opportunities for a distributor to cross-subsidise the connected generator or a directly connected generator of over 250MW?**

39. The Commerce Commission has previously noted (for instance in Decisions 541 and 629) that the potential for cross-subsidisation between generation activities and a lines business is of particular concern where a generator has the potential to connect generation to a local distribution network. However, none of the generating assets of Mighty River Power are currently connected to AIAL's distribution network. There is no current proposal for Mighty River Power to connect any future generation assets to AIAL's network.
40. The Commerce Commission has also taken the view (for instance in Decisions 517 and 629) that an electricity lines business could be used to cross-subsidise a generator's generation activities. This could occur through the terms of a use of system agreement negotiated between the generator and the distribution network, which did not provide a commercial return to the network operator, with the opportunity for the negotiation of such an agreement being influenced by the presence of a cross-involved person having a material influence within the two companies.
41. We submit that, provided that Mr Miller complies with the proposed conditions of exemption set out above, then AIAL would have no incentives or opportunities to cross-subsidise Mighty River Power's generation activities from its lines business. In particular:
- (a) The proposed conditions would prohibit Mr Miller from participating in any discussions or decision making in either Mighty River Power or AIAL in relation to the negotiation, and ongoing administration of, a use of system

agreement between Mighty River Power and AIAL in relation to AIAL's network. This will limit the risk that Mr Miller's involvements in AIAL and Mighty River Power could lead to the negotiation of a use of system agreement between AIAL and Mighty River Power that does not provide a commercial return to AIAL and therefore would cross-subsidise Mighty River Power's generation activities;

- (b) AIAL's equity securities are quoted on the New Zealand Exchange Limited (NZX). The NZX Listing Rules prohibit directors of such companies from voting or being included in a quorum where they are "interested" in a transaction (Rule 3.4.3). This would prevent Mr Miller in his capacity as a director of AIAL from voting or being included in a quorum in the event that Mighty River Power proposed to supply in future AIAL's own electricity requirements, or negotiate an amended use of systems agreement with AIAL.

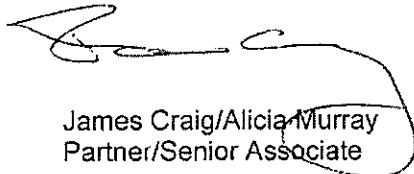
**Would the exemption, in respect of an involvement, permit a relationship between a distributor and a retailer or generator which is not at arm's length?**

42. Section 76 and Schedule 3 of the Act deal with the arm's length rules. As set out above, Mighty River Power will not be a "connected retailer" under the definition in section 76(3) of the Act, as a result of Mr Miller's position as director of both Mighty River Power and AIAL. This is because Mighty River Power (through Mercury Energy) retails less than 75GWh of electricity per year on AIAL's distribution network. Therefore, the relationship will be at arm's length for the purposes of Part 3 of the Act.

**DECLARATION**

43. **Attached** in support of this application is a Declaration completed by Mr Miller as applicant in the prescribed form.
44. Please let us know if you have any questions.

Yours faithfully  
SIMPSON GRIERSON



James Craig/Alicia Murray  
Partner/Senior Associate



**DECLARATION**

**THIS APPLICATION** is made by Mr James Bruce Miller.

I hereby confirm that:

- all the information requested by the Electricity Authority is provided;
- all relevant information known to the applicant is provided; and
- all information provided is true and correct as at the date of this application.

I undertake to advise the Authority immediately of any material change in circumstances relating to the application.

Date: 21 March 2012

Signed by:

  
James Bruce Miller

**CONFIDENTIAL SCHEDULE**

**Mighty River Power Airport Customers**

Customer Name:

**Confidential information redacted**