

DRAFT DECISION

Decision No. 1

Draft decision pursuant to the Electricity Industry Act 2010 (Act), in respect of a request for an exemption under section 90 of the Act relating to the involvement of a person in a distributor and a connected generator or a connected retailer.

- Applicant** Mighty River Power Limited (MRPL) and Mr James Miller (Mr Miller), on behalf of Mr Miller.
- Summary of application:** Mr Miller is a director of Auckland International Airport Limited (a distributor). It is proposed that Mr Miller be appointed as a director of MRPL. That appointment would give rise to a prohibited involvement in terms of Part 3 of the Act. The application requests that the Electricity Authority (Authority) exempt, under section 90(1)(a) of the Act, the involvement of Mr Miller from the application of Part 3 of the Act.
- Summary of draft decision:** While the Applicant sought an exemption under section 90(1)(a), the Authority proposes to grant Mr Miller an exemption under section 90(1)(b). The exemption is from compliance with sections 75, 77 to 79 and 88 of the Act, and would be subject to the conditions set out in the draft Notice of Exemption attached as appendix 1.
- Date of draft decision:** 23 April 2012.
- Date of exemption:** It is proposed that the exemption takes effect from 1 May 2012.

Introduction

1. Mr James Miller is currently a director of Auckland International Airport Limited (AIAL). AIAL is a distributor in terms of the Electricity Industry Act 2010 (Act) because it is engaged in the business of conveying electricity on lines (not being lines that are part of the national grid). It is proposed that Mr Miller be appointed as a director of Mighty River Power Limited (MRPL), which is an electricity generator and retailer.
2. On 21 March 2012, the Electricity Authority (Authority) received an application (Application) from MRPL and Mr Miller jointly on behalf of Mr Miller, requesting that the Authority grant an exemption under section 90 of the Act in respect of Mr Miller's proposed appointment as a director of MRPL while Mr Miller remains a director of AIAL.
3. On 30 March 2012, the Authority received further information from the Applicant which clarified that the exemption is requested under section 90(1)(a) of the Act. That is the Applicant requests that Mr Miller's involvement be exempted from the application of Part 3.
4. In the absence of an exemption under section 90, the appointment of Mr Miller as a director of MRPL would mean that Mr Miller would breach the ownership separation requirement in section 75 of the Act.

What the Applicant requests

5. The Applicant has requested, on behalf of Mr Miller, that the Authority grant an exemption under section 90(1)(a) of the Act to exempt Mr Miller's proposed involvement in MRPL from the application of Part 3 of the Act. Mr Miller has requested the exemption be granted subject to the following conditions:
 - (a) While Mr Miller is a director of both AIAL and MRPL, Mr Miller will not participate in any discussions or decision-making by MRPL and/or AIAL regarding matters that relate to or could affect or favour the supply of electricity by MRPL (or disadvantage any other business selling electricity on AIAL's network other than MRPL) on AIAL's electricity distribution network or the provision of electricity lines services by AIAL to MRPL, 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 MRPL 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 MRPL (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 MRPL. It does not extend to any other interest or future cross-involvement of Mr Miller.

Electricity Authority procedures

General

6. For the purposes of considering the Application the Authority has appointed a committee (Committee) comprising Dr Brent Layton, Chair of the Board of the Authority, and Mr Carl Hansen, Chief Executive of the Authority, under clause 14(1)(b) of Schedule 5 of the Crown Entities Act 2004.
7. The Authority has delegated to the Committee, under section 73(1)(c) of the Crown Entities Act, the power to consider and determine whether to grant an exemption under section 90 to Mr Miller, including to determine any terms and conditions that the Committee reasonably considers are necessary to give effect to the purpose of Part 3 of the Act.

Process the Authority follows to consider an exemption application

8. The Authority has issued guidelines on Part 3 of the Act (Guidelines).¹ The Guidelines set out the process the Authority follows in relation to a request for an exemption.
9. In summary, the Authority adopts the following process in relation to an application for an exemption:
 - (a) receive and register the application;
 - (b) publish the application on the Authority's website;
 - (c) assign investigative staff;
 - (d) investigate the application (which may include interviewing and seeking comment from relevant parties);
 - (e) publish a draft report on the Authority's website and seek comment from interested parties, including comment on proposed terms and conditions (if any);
 - (f) make a decision;
 - (g) publish decision on the Authority's website;
 - (h) publish notice of exemption in the *Gazette* (if applicable); and
 - (i) include in register of current exemptions (if applicable).
10. The Authority has completed steps (a) to (d) above. This document is part of fulfilling step (e).

¹ <http://www.ea.govt.nz/act-code-regs/part-3-of-the-act/>.

Criteria used by the Authority to consider a request for an exemption

11. The Guidelines state that when considering whether to grant an exemption, the Authority will consider whether doing so would be contrary to the purpose of Part 3 and the Authority's objective set out in section 15 of the Act. That objective is to "promote competition in, reliable supply by, and the efficient operation of, the electricity industry for the long-term benefit of consumers".
12. In addition to the statutory criteria in section 90(2) of the Act, the Guidelines state that the Authority will take into account the following:
 - (a) whether the exemption, in respect of a business or involvement, will create incentives or opportunities for a distributor to cross-subsidise the connected generator or a directly connected generator of over 250MW; and
 - (b) whether the exemption, in respect of a business or involvement, will permit a relationship between a distributor and a retailer or generator which is not at arm's-length.
13. The Authority considers that the first of the matters above (regarding cross-subsidisation) is a more detailed articulation of a potential issue relevant to determining whether the criteria in section 90(2) are met, as well as a way to assess whether the purpose specified in section 72(1)(a) is given effect.
14. The Authority considers that the second matter (regarding arms-length relationships) reflects that, as referred to in section 90(4), the Authority may grant an exemption on terms and conditions it considers reasonably necessary to achieve the purpose of Part 3, in particular the purpose specified in section 72(1)(b).
15. Finally, the Guidelines also state that in relation to the statutory criteria and the above matters, the Authority will consider factors such as:
 - (a) the relevant market(s) in the electricity industry;
 - (b) the nature of any incentives or opportunities created;
 - (c) the temporal nature of any incentives or opportunities created;
 - (d) the nature of any relationship which is not at arm's-length; and
 - (e) the temporal nature of any relationship which is not at arm's-length.

Parties

Mr Miller

16. Mr Miller is currently a director of AIAL. On 20 March 2012, the Minister for State-owned Enterprises, the Hon. Tony Ryall, announced his intention to appoint Mr Miller to the Board of MRPL, on or after 1 May 2012 (pending the Authority exempting Mr Miller prior to that date).
17. Mr Miller resigned as a director of Vector Limited (Vector) (a distributor) on 20 March 2012.

AIAL

18. AIAL owns and operates Auckland Airport, the principal gateway for more than 70% of visitors to New Zealand. 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.
19. 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.
20. 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's citywide network at the perimeter of the airport.
21. AIAL distributes electricity to 376 consumers, spread over 491 ICPs, at the airport. Of the 102 GWh per annum distributed over AIAL's network, 31.2 GWh is for AIAL's own use.
22. Electricity retailers TrustPower, Genesis Power Limited, Contact Energy Limited, Meridian Energy Limited, Simply Energy and Mercury Energy (MRPL's retail brand) each have access to AIAL's network in accordance with a standardised use-of-system agreement, and compete to sell electricity to consumers connected to AIAL's network.
23. The market shares of those retailers across AIAL's network in February 2012 are set out below:

Retailer	% kWh reconciled to retailer
Contact	[]
Genesis	[]
Mercury	[]
Meridian	[]
Simply	[]
TrustPower	[]
TOTAL	100.00%

24. The existing directors of AIAL are John Brabazon, Richard Didsbury, Brett Godfrey, James Miller, Keith Turner, Henry van der Heyden and Joan Withers. As noted below, Joan Withers is also the Chair of the Board of MRPL.

MRPL

25. MRPL is an electricity generator and retailer, which was formed as a result of the division of the Electricity Corporation of New Zealand into three separate companies in April 1999. MRPL is currently a State-Owned Enterprise but, pending the enactment of the Mixed Ownership Model Bill (2012), the Government has announced that it intends to sell up to 49% of its shares in MRPL.
26. MRPL 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.

27. Mercury Energy, MRPL's electricity and gas retail division, retails electricity in various regions in New Zealand.
28. Relevant to this decision, Mercury Energy supplies electricity to various consumers at AIAL, and is the [] largest retailer on the AIAL network. []
29. The existing directors of MRPL 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 it is intended that Mr Miller will replace him.

Joan Withers

30. As noted above, Joan Withers is the Chair of the Board of MRPL and is also a director of AIAL. On 31 July 2009, the Commerce Commission granted Ms Withers an exemption (subject to certain conditions) from compliance with section 17(2)(b) of the Electricity Industry Reform Act 1998 in respect of her directorships of both MRPL and AIAL (Commerce Commission Decision number 676). Section 144 of the Electricity Industry Act continues the exemption and the corresponding provisions of the Electricity Industry Act apply.

The Statutory Framework

Part 3 of the Act

31. Section 72 of the Act provides that the purpose of Part 3 is to promote competition in the electricity industry:
 - (a) by prohibiting a person who is involved in a distributor from being involved in a generator where that may create incentives and opportunities to inhibit competition in the electricity industry; and
 - (b) by restricting relationships between a distributor and a generator or retailer, where those relationships may not otherwise be at arm's-length.
32. Implicit in the purpose outlined above is that the involvements to which Part 3 apply, and relationships between parties that are involved, may inhibit competition in the electricity industry.
33. The solution, as implemented in Part 3 of the Electricity Industry Act (and, before that, in the Electricity Industry Reform Act 1998), is to require ownership separation, corporate separation, and the implementation of other safeguards such as arm's-length rules and other requirements relating to use-of-system agreements.
34. To assist in determining when an interest or involvement will give rise to concerns under Part 3 of the Act, Schedule 2 of the Act lists certain types of interests and involvements that are excluded from the application of the separation rules in Part 3. Schedule 2 gives an indication of the type of involvements that are seen to give rise to the possibility of inhibiting competition.
35. It also lists some involvements that are not taken into account. These include interests in distributors and generators and other interests that arise only out of financial relationships, or other benign arrangements, such as industry service providers that are only involved because of their position.

Section 90

36. Section 90(1) of the Act provides that the Authority may, by notice in the *Gazette*, exempt:
 - (a) any business or involvement from the application of Part 3; or
 - (b) any person from compliance with any provisions of Part 3.
37. Section 90 recognises that the policy that Part 3 is intended to implement will not always be compromised by a person's involvement in a distributor on the one hand, and a generator or retailer on the other.
38. However, in respect of interests and involvements that are to be counted, section 90(2) provides that the Authority may grant an exemption only if it is satisfied that:
 - (a) the exemption will either promote, or not inhibit, competition in the electricity industry; and
 - (b) the exemption will not permit an involvement in a distributor and a generator or retailer that may create incentives and opportunities to inhibit competition in the electricity industry.
39. The Authority may grant an exemption on any terms and conditions that it reasonably considers are necessary to give effect to the purpose of Part 3.
40. This draft decision is the first time that the Authority has had the opportunity to consider the interpretation and application of section 90.
41. In light of that, the Authority has considered its approach to determining whether an exemption under section 90(1)(a) or section 90(1)(b) is appropriate in any given case.
42. As a general principle, the Authority's view is that any exemption should be the minimum necessary to permit a person to be involved in both a distributor and a generator or retailer but otherwise seek to preserve the application of Part 3.

The difference between a section 90(1)(a) exemption and a section 90(1)(b) exemption

43. In investigating the Application, the Authority asked the Applicant why an exemption was sought in terms of section 90(1)(a) (ie for Mr Miller's involvement) rather than under section 90(1)(b) (exemption from compliance with particular provisions). In particular, the Authority sought the Applicant's views of the effect of granting an exemption under each provision.
44. The Applicant responded that an application had been made for an exemption of the involvement under section 90(1)(a) because, by virtue of clause 4(1)(a) of Schedule 2, it would mean that, for the purposes of Part 3, no account would be taken of the involvement. Because sections 75, 77 to 79 and 88 only apply when there is an involvement, an exemption under section 90(1)(a) would mean that Mr Miller's proposed involvement would not cause those provisions to apply.
45. In relation to the effect of an exemption under section 90(1)(b), the Applicants reserved their position. However, the Applicant stated that, if an exemption was obtained for Mr Miller from compliance with sections 77 to 79 and 88, under section 90(1)(b) on the conditions sought, then it followed that Mr Miller's involvement in a connected retailer for the purpose of those specific provisions "*should not be taken into account when considering the application of those provisions*

to the other directors of AIAL. We note in this respect that clause 4(1)(a) of Schedule 2 applies to an exemption by the Authority under section 90 generally (which would include section 90(1)(b) and not just to an exemption under section 90(1)(a))."

46. The Authority has considered those views further below.

Section 90(1)(a)

47. Section 90(1)(a) of the Act provides that the Authority may exempt "any business or involvement" from the application of Part 3. That is, the exemption relates to a business, generally, or an involvement, generally.
48. The effect of an exemption under section 90(1)(a) is that the business or involvement is not taken into account in determining whether any of the provisions in Part 3 apply to a business or to a person (such as a director of a distributor): clause 4(1)(a) of Schedule 2 of the Act provides that no account is to be taken of a person's business or involvement if the business or involvement is exempted under section 90.
49. Because the involvement is not taken into account for the purposes of determining whether the Part 3 obligations apply to other persons (such as directors of a distributor with a connected generator or connected retailer, as referred to in section 77 of the Act), the consequence of an exemption being granted in respect of an involvement (or business) in section 90(1)(a) is that other persons may obtain the benefit of the exemption in terms of being excused from complying with particular provisions in Part 3.

Section 90(1)(b)

50. Section 90(1)(b) provides that the Authority may exempt any person from compliance with any provisions of Part 3.
51. The effect of such an exemption is that the person to whom the exemption applies is not required to comply with the relevant provisions of Part 3.
52. Clause 4(1) of Schedule 2 of the Act provides that no account is to be taken, for the purposes of Part 3, of a person's business or involvement if the business or involvement is exempted by the Authority under "section 90". That is, clause 4(1) does not, on its face, differentiate between an exemption under section 90(1)(a) and an exemption under section 90(1)(b).
53. However clause 4(1) clearly refers to an exemption of "a business or involvement". Only section 90(1)(a) provides for the exemption of a business or involvement. In contrast, section 90(1)(b) refers to an exemption for a person "from compliance with any provisions of" Part 3.
54. The Authority's view is that, if a person is exempted under section 90(1)(b) of the Act from compliance with certain provisions, his or her involvement must still be taken into account in determining whether the provisions of Part 3 of the Act apply to other persons, businesses, or involvements.

Analysis of the Application

Why is an exemption needed?

Section 75 prohibition

55. In the absence of an exemption, section 75 would prohibit the appointment of Mr Miller to the Board of MRPL while he remains a director of AIAL, as set out below.
56. Section 75 of the Act provides:
- "(1) *A person who is involved in a distributor must not be involved in 1 or more generators that have a total capacity of more than 250 MW that is generated by 1 or more generating plants that are directly connected to the national grid.*
- (2) *To avoid doubt, generation connected to a distribution network is not directly connected to the national grid.*"
57. Section 5 of the Act defines a distributor as being "a business engaged in distribution". "Distribution" is defined as meaning "the conveyance of electricity on lines other than lines that are part of the national grid". AIAL owns the electricity distribution network for Auckland Airport. AIAL is, therefore, a business engaged in distribution and a distributor.
58. Section 5 defines a generator as "a business engaged in generation", and generation means "the generation of electricity that is fed into the national grid or a network". MRPL has a total generating capacity of 1,601 MW and is, therefore, a business engaged in generation and a generator.
59. Section 74 of the Act provides that a person is "involved in" a distributor, a generator, or a retailer if the person, amongst other things, "has material influence over a business that does any of those things" (ie distribution, generation or retail).
60. "Material influence" is defined in clause 7 of Schedule 2 of the Act. Clause 7 provides that "a director or manager of a person that carries on the business" is deemed to have material influence over a business.
61. Mr Miller is a director of AIAL and, and such, is deemed to have material influence over a distributor (AIAL). Upon his appointment to the Board of MRPL, Mr Miller would also be deemed to have material influence over a generator (MRPL).
62. On this basis, Mr Miller is a person involved in a distributor and, if Mr Miller is appointed to the Board of MRPL as proposed, he would also be involved in a generator and a retailer. This would be contrary to the ownership separation rule in section 75.

Consequential matters – sections 77 to 79 and section 88

63. If an exemption is granted to Mr Miller so that he may be appointed to the Board of MRPL without breaching the prohibition in section 75, this gives rise to the need to comply with other obligations in Part 3 for Mr Miller, for the other AIAL directors and, in relation to section 78, MRPL and persons involved in MRPL.

64. As identified in the Application, sections 77 to 79 and 88 of the Act apply to each director of a distributor in respect of which there is a connected retailer or a connected generator.
65. MRPL is not a connected generator because it does not have any generation connected to AIAL's network.
66. However, MRPL is a "connected retailer" for the purposes of sections 77 to 79 and 88. A connected retailer, in relation to a distributor, is 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 other person involved in the distributor is involved.
67. MRPL, through its retail brand Mercury Energy, retails more than 5 GWh of electricity to customers connected to AIAL's distribution network. Therefore, MRPL is a connected retailer in respect of AIAL, for the purposes of the Application.
68. As such, sections 77 to 79 and 88 of the Act would apply to Mr Miller and to each of the directors of AIAL if the proposal to appoint Mr Miller to the Board of MRPL proceeds. Section 78 would also apply to MRPL and persons involved in MRPL. Those sections require, in summary (relevant to the Application):
 - (a) *section 77*: every director of a distributor in respect of which there is a connected retailer or connected generator must ensure that the distribution business has a comprehensive written use-of-systems agreement between the distributor and the connected retailer or connected generator, and that the terms of that agreement meet certain requirements;
 - (b) *section 78*: a distributor and a connected generator or a connected retailer 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;
 - (c) *section 79*: every director of a distributor that has a connected retailer must ensure that any rebates or dividends or similar payments made do not discriminate between customers of the connected retailer and customers of other retailers where those customers are connected to the distributor's networks; and
 - (d) *section 88*: each director of a distributor referred to in section 77(1) must ensure that the distributor discloses to the Authority the quantity of electricity sold each financial year by connected retailers to customers who are connected to its local network.

The Applicant's submissions

69. In its Application the Applicant submits that "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."
70. In respect of any incentives and opportunities created in the national electricity and wholesale market the Applicant submits:

"MRPL'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."

71. In respect of the electricity retailing markets the Applicant submits that the focus of the Authority's enquiry should be on AIAL's distribution network. The Applicant states:

"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."

72. Finally, in respect of the regional electricity distribution markets, the Applicant submits that, as AIAL's network is a natural monopoly, granting the exemption would not affect the level of existing competition and would therefore not create incentives or opportunities to inhibit competition in the market.

73. In its 30 March 2012 correspondence, the Applicant states that Mr Miller should be exempted from compliance with sections 77 to 79 and 88 of the Act because, under the conditions of exemption sought, Mr Miller would not have visibility of the terms on which MRPL is supplying electricity over the AIAL network. As such, he would not be able to comply with the obligations imposed on him in those sections. For example, he would not be in a position to sign a certificate for the purposes of section 77(4) stating that the terms in the AIAL use-of-systems agreement were a true and fair view of the terms on which line function services were supplied.

74. That correspondence also provides the reasons why the Applicant considers that the other directors of AIAL with no involvement in MRPL should not have to comply with sections 77 to 79 and 88 of the Act if the exemption was granted on the proposed conditions. In summary:

- (a) On the basis that the proposed conditions would exclude Mr Miller from being involved in decisions relating to MRPL, the other directors would have no incentive to favour MRPL in the supply of electricity over the MRPL network. In support of this, it is stated that MRPL is not supplying the bulk of electricity over the AIAL network such that AIAL would have no reason to favour its interests; and
- (b) In circumstances where the other directors of AIAL have no reason to favour MRPL in the supply of electricity over the AIAL network, it would be unduly onerous to require those directors to comply with the additional requirements in sections 77 to 79 and 88. This is especially the case in circumstances where the penalties for breach of these sections are serious (ie summary conviction and substantial fines).

The Authority's approach to the analysis

75. In order to assess whether the criteria in section 90(2) of the Act are met, and in light of the Guidelines, the Authority has set out its analysis as follows:

- (a) Identification of the relevant market or markets;

- (b) Consideration of whether granting an exemption would either promote, or not inhibit, competition in the electricity industry (section 90(2)(a));
- (c) Consideration of whether granting an application would create incentives and opportunities to inhibit competition in the electricity industry (sections 72(1)(a) and 90(2)(b));
- (d) Discussion regarding opportunities for a distributor to cross-subsidise the connected generator or a directly connected generator of over 250MW (section 75 and Guidelines); and
- (e) Consideration of whether the exemption, in respect of a business or involvement, will permit a relationship between a distributor and a retailer or generator which is not at arm's-length (section 72(1)(b) and Guidelines).

The relevant markets

- 76. Both statutory criteria in section 90(2) of the Act include a reference to competition in the electricity industry. In order to assess how the granting of an exemption pursuant to the Application would affect competition in the electricity market it is necessary to identify the relevant market or markets.
- 77. Consistent with the view expressed in the Application, the Authority is of the view that the markets relevant to the Application are the national electricity wholesale market, the electricity retail market corresponding with AIAL's network, and the electricity distribution market corresponding with AIAL's network.
- 78. In the context of this analysis, any issues with competition are likely to arise (if anywhere) in the electricity retail market corresponding with AIAL's distribution network. The Authority therefore initially focuses on this market and addresses the other two markets later in the decision.

Will the exemption promote, or not inhibit, competition in the retail market (section 90(2)(a))?

- 79. Mr Miller and MRPL did not assert in the application that an exemption of Mr Miller's involvement, on the conditions proposed, would promote competition. The Authority similarly does not consider that there are any grounds to suggest that an exemption of the involvement, including on the conditions proposed, would promote competition in the electricity retail market corresponding with AIAL's network.
- 80. In relation to whether the exemption sought would not inhibit competition, as outlined above, if Mr Miller's involvement in MRPL is exempted, that involvement cannot be taken into account for the purposes of Part 3. The effect is that:
 - (a) Mr Miller will not have to comply with sections 77 to 79 and 88; and
 - (b) AIAL and the remaining AIAL directors, and MRPL and the persons involved with MRPL, may disregard Mr Miller's involvement for the purposes of determining whether they have obligations under those sections.
- 81. That is, the exemption of the involvement would apply not only to Mr Miller, but also to AIAL, MRPL, and persons involved in these businesses. The proposed conditions of the exemption, on the other hand, would only apply to Mr Miller.

82. The conditions proposed would exclude Mr Miller from discussions and decision-making relating to both AIAL and MRPL, and this would leave AIAL in the same position as a company that is a distributor without a director with cross involvement. The remaining directors of AIAL are required to fulfil their statutory duties to act in the best interests of AIAL.
83. The effect of those conditions goes some way towards satisfying the Authority that the exemption would not inhibit competition.
84. However, the Authority does not need to come to a final view on whether an exemption for Mr Miller's involvement will not inhibit competition. This is because, for the reasons set out in paragraphs 86 to 94 below, the Authority considers that exempting Mr Miller's involvement will result in residual incentives or opportunities for the directors of AIAL to favour MRPL. In light of that, the Authority cannot grant the exemption requested.
85. However, the Authority proposes to exempt Mr Miller from compliance with sections 75, 77 to 79 and 88 of the Act. The Authority is satisfied that such an exemption, which would be granted under section 90(1)(b) of the Act, would not inhibit competition in the electricity retail market corresponding with AIAL's network.

Will the exemption not permit an involvement that may create incentives and opportunities to inhibit competition in the retail market (section 90(2)(b))?

86. The effect of the proposed conditions would be that, while acting as a director of AIAL, Mr Miller would not be able to participate in discussions or decision-making relating to matters involving MRPL.
87. If an exemption is granted with those conditions, this would go a considerable way to removing any incentives or opportunities that could be said to arise from Mr Miller's directorships of AIAL and MRPL. All company directors are subject to New Zealand company law and are under a duty to act in the best interests of the company of which they are a director.
88. However, the Authority remains concerned that, while the proposed conditions should in theory address all incentives and opportunities to inhibit competition, granting an exemption will result in some residual incentives or opportunities for the directors of AIAL to favour MRPL.
89. The Authority considers that those residual incentives or opportunities could be addressed by ensuring that the remaining directors of AIAL, MRPL and people involved in MRPL are required to comply with the safeguards in sections 77 to 79 and 88 of the Act.
90. For that reason, the Authority considers that the criterion in section 90(2)(b) is made out in respect of an exemption granted under section 90(1)(b), but not under section 90(1)(a).
91. The Authority sought the views of AIAL and MRPL in respect of whether they would be able to comply with the safeguards in sections 77 to 79 and 88. Both companies indicated their willingness and ability to comply if an exemption was granted under section 90(1)(b).
92. The Authority considers that compliance with the obligations in sections 77 to 79 and 88 would not be onerous. Ensuring these obligations are met will instil confidence in other retailers and

consumers on the AIAL network that the involvement of Mr Miller as a director of AIAL and MRPL would not lead AIAL to favour MRPL over other retailers.

93. The Authority considers that the incentives or opportunities that may be created by Mr Miller's directorships in both AIAL and MRPL can be effectively addressed by:
- (a) limiting Mr Miller's participation in matters relating to electricity retailing or distribution services between those companies, or between AIAL and any other electricity retailer; and
 - (b) granting the exemption under section 90(1)(b) with the effect that the remaining directors of AIAL, and MRPL and those involved in MRPL, are required to comply with their respective obligations in sections 77 to 79 and 88.
94. Provided sections 77 to 79 and 88 apply, these incentives and opportunities are sufficiently addressed. The Authority therefore considers that the criterion in section 90(2)(b) is satisfied.

Incentives or opportunities for cross subsidisation

95. The Guidelines state that, in assessing an application, the Authority will consider whether the exemption would, in respect of the business or involvement, create opportunities or incentives for a distributor to cross-subsidise the connected generator or a directly connected generator of over 250 MW.
96. The Authority considers that granting Mr Miller an exemption from compliance with sections 75, 77 to 79, and 88, subject to certain conditions, would be unlikely to, in respect of his involvement with AIAL and MRPL, create incentives or opportunities for a distributor to cross-subsidise the connected generator or a directly connected generator of over 250 MW because:
- (a) MRPL has no generation directly connected to AIAL's network and, therefore, is not a connected generator;
 - (b) the proposed conditions prevent Mr Miller from participating in any future discussions or decision-making that relates to or could affect or favour the retail of electricity by MRPL (or disadvantage any other retailer other than MRPL) on AIAL's network or the provision of distribution services to MRPL.

Permitting a relationship which is not at arm's-length

97. The Guidelines state that in assessing an application, the Authority will consider whether the exemption would, in respect of a business or involvement, permit a relationship between a distributor and a retailer or generator which is not at arm's-length.
98. In most circumstances where an exemption is required from the ownership separation provisions of the Act, a relationship will be created that will ultimately not be at arm's length. In this case, any potential effects of the relationship not being at arm's length can be tempered by the condition that the Applicant would not participate in any future discussions or decision-making that relates to or could affect or favour the retail of electricity by MRPL (or disadvantage any other retailer other than MRPL) on AIAL's network or the provision of distribution services to MRPL.

Other markets

99. This section considers competition in the national wholesale electricity market and the electricity distribution market corresponding with AIAL's network in light of the proposal to grant an exemption under section 90(1)(b).

National wholesale market

100. MRPL's generation assets are not directly connected to AIAL's distribution network, nor is it intended that they will be in the future. Therefore, granting Mr Miller an exemption from compliance with sections 75, 77 to 79, and 88 would not, in respect of his involvement with AIAL and MRPL, create incentives or opportunities to inhibit competition in the national electricity wholesale market.

Electricity distribution market corresponding with AIAL's network

101. Local electricity distribution networks are characterised by being local natural monopolies. Granting Mr Miller an exemption from compliance with sections 75, 77 to 79, and 88 would not, in respect of his involvement with AIAL and MRPL, create incentives or opportunities to inhibit competition in the electricity distribution market corresponding with AIAL's network.

Draft decision

102. The Authority proposes to grant Mr Miller an exemption under section 90(1)(b) from compliance with sections 75, 77 to 79 and 88 of the Act, subject to the conditions set out in the draft Notice of Exemption attached as appendix 1.
103. This is because the Authority is satisfied that an exemption under section 90(1)(b) will:
- (a) not inhibit competition in the relevant markets; and
 - (b) not permit an involvement in a distributor and a generator or retailer that may create incentives and opportunities to inhibit competition in the electricity industry.

Conditions

104. As a condition of Mr Miller's exemption, the Applicant proposed that the exemption expire when the Authority publishes on its website Mr Miller's written confirmation that his cross-directorship has ceased. The Authority does not consider that it is able to impose such a condition. This is because, under section 90(5) of the Act, an exemption must be revoked by giving notice to that effect in the *Gazette*. Under the proposed conditions, Mr Miller must confirm to the Authority when his cross-directorship ceases, but his exemption would not expire until it is revoked by the Authority by a notice in the *Gazette*.
105. Otherwise the Authority is satisfied that the proposed conditions outlined in the draft Notice of Exemption are necessary to give effect to the purposes of the Act.
106. Finally, the Authority is satisfied that the proposed exemption, on the proposed conditions, is consistent with the purpose of Part 3 of the Act and the Authority's statutory objective.

Comments sought

107. The Authority seeks comments from interested parties on the Authority's proposal, including comments on the terms and conditions proposed. The Authority requests that comments are provided no later than 5 pm on Thursday, 26 April 2012.
108. After taking any comments into account, the Authority will make its final decision on the Application and publish a notice of exemption (if applicable) in the *Gazette*.

Appendix 1

Notice of Exemption

Exemption issued to Mr James Miller pursuant to section 90(1)(b) of the Electricity Industry Act 2010

Pursuant to section 90(1)(b) of the Electricity Industry Act 2010 (**Act**), the Electricity Authority (**Authority**), grants an exemption to Mr James Miller (**Mr Miller**) from compliance with sections 75, 77 to 79 and 88 of the Act, in relation to the proposed appointment of Mr Miller as a director of Mighty River Power Limited (**MRPL**) while Mr Miller is also a director of Auckland International Airport Limited (**AIAL**).

The exemption is subject to the following conditions:

1. While Mr Miller is a director of both AIAL and MRPL:
 - (a) Mr Miller must not participate in any discussions or decision-making by MRPL and/or AIAL regarding matters that relate to or could affect or favour the supply of electricity by MRPL (or disadvantage any other business selling electricity on AIAL's network other than MRPL) on AIAL's electricity distribution network or the provision of electricity lines services by AIAL to MRPL, 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 MRPL to any new, or existing, consumers on AIAL's electricity distribution network;
 - (b) Mr Miller must not disclose the outcomes of any discussions or decision-making by AIAL to MRPL (and vice versa) on the matters referred to in paragraph (a).
2. Mr Miller must confirm to the Authority, in writing, that the cross-directorship to which this exemption applies has ceased within one calendar month of the cross-directorship ceasing to exist.
3. The exemption is specific to the cross-directorship created through Mr Miller's involvement in AIAL and MRPL. It does not extend to any other interest or future cross-involvement of Mr Miller.

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