

Electricity Industry Reform Amendment Bill

Government Bill

As reported from the Commerce Committee

Commentary

Recommendation

The Commerce Committee has examined the Electricity Industry Reform Amendment Bill and recommends that it be passed with the amendments shown.

Introduction

This bill amends the Electricity Industry Reform Act 1998. The original Act required full separation of the ownership of electricity lines and of electricity supply businesses. The Act was amended in 2001 and 2003 to allow electricity lines businesses to own generation up to specified quantities if they complied with corporate separation and arm's-length rules. This bill seeks to encourage lines companies to invest in permitted generation, particularly renewable generation. It proposes to achieve this by

- relaxing some of the corporate separation and arm's-length rules relating to generation and retailing
- allowing electricity lines businesses to sell more electricity

- allowing electricity lines businesses to hedge the output of their generation
- allowing electricity lines businesses to invest in generation and retail without limit outside their own lines areas.

This commentary focuses on the major issues we examined and the amendments recommended. We also recommend amendments to clarify the intent of the bill and other minor changes which are not discussed.

Submissions not leading to amendment

Submissions fell mainly into two opposite schools of thought: one of them that nothing short of repeal of the entire Electricity Industry Reform Act would suffice, and the other that the amendments in the bill are more than is needed.

Complete repeal of the Act

Several submitters suggested that the bill does not go far enough and some advocated the complete repeal of the Electricity Industry Reform Act to remove all ownership and corporate separation and arm's-length restrictions. They argued that continuing restrictions were unnecessary and imposed compliance costs, thus discouraging investment.

Amendments go too far

Several other submitters were concerned that the bill goes too far, and that relaxing the corporate separation and arm's-length rules would create incentives and opportunities for lines businesses to inhibit competition in the electricity industry.

Corporate separation and arm's-length rules

Involvement in lines business

The ownership separation requirements are triggered when a person is involved in a lines business that is in breach of the connected generation cap rule in new section 17A, or in breach of the connected customer selling cap rule in new section 17C. The corporate separation and arm's-length rules apply to an electricity business or a person in-

volved in a business, if the business or person has an involvement in connected generation above the 10MW threshold in new section 17D.

We recommend inserting new section 7A (clause 7) to make it clear that only the proportion of generation that is owned by the lines business is counted towards its connected generation. New section 7 (clause 7) defines “involved” in the context of involvement in an electricity business. There was some concern that the definition of “involved” would include the entire quantity of connected generation, even if the lines business owned only a proportion of that generation. This definition is important for the calculation of the connected generation and customer selling cap rules.

We recommend amending section 19(1) and new section 19(1A) (clause 11) to disregard generation and conveyance of less than 5GWh per annum and retail sales of less than that amount, to allow for load growth in smaller networks since the principal Act’s introduction. The bill as introduced, by comparison, disregarded involvement if the line conveyed less than 2.5GWh per annum.

We recommend amending new section 17B (clause 8) to make it clear that generation disregarded for the purpose of calculating the connected generation cap rule in new section 17A would nevertheless be counted towards the threshold for corporate separation and arm’s-length rules in new section 17D. Some existing exemptions granted by the Commerce Commission would therefore continue to apply.

New section 17A (clause 8) appears to render unlawful some existing lawful investments in generation under section 5(2)(e) of the principal Act. We recommend amending new section 17A to make it clear that only generation with a total capacity greater than 5MW is counted towards the connected generation cap.

New section 17D (clause 8) sets the threshold for corporate separation and arm’s-length rules at involvements with more than 10MW in generation, or retailing more than 87,600MWh, which equates to 10MW operated at 24 hours for 365 days per annum. As the latter threshold is unnecessary, in the light of the former, we recommend that it be deleted.

Anti-competitive risks

Some submitters argued that raising the threshold for corporate separation and arm's-length rules from 5 to 10MW increases the risk of lines businesses favouring their own retailing business. We agree that fair and equitable access to lines for competing retailers is important. We recommend inserting new section 17EA (clause 8) to provide that a lines business that is involved in 5MW of connected generation and selling more than 5GWh per annum of electricity to connected customers must have a comprehensive, written use-of-systems agreement with its retail arm. This agreement should not discriminate in favour of that business, and it must be published on the generator's Internet site. Failure to comply with these requirements would be an offence under new section 17EA(4).

Interpretation**Definition of "local network"**

The current definition of "local network" does not give adequate guidance as to the boundaries of a local network and what it includes and excludes. We recommend amending the definition of "local network" to give clearer guidance on local network boundaries.

Definition of "manager"

We recommend inserting a new definition of "manager" to clarify that it does not include a director. The current definition of "manager" in the principal Act includes directors, which is inconsistent with some of the arm's-length rules in proposed new Schedule 1, set out in the Schedule to this bill. For example, rule 9 seems to prohibit common management while permitting cross-directors.

As a consequence of this amendment, we recommend amending the definition of "material influence" contained in section 11(1)(a) of the principal Act by inserting new section 7B (clause 7) to include a separate reference to managers and directors, and replacing Schedule 1 of the principal Act with the arm's-length rules (incorporating both directors and managers) set out in the Schedule to the bill.

Appendix

Committee process

The Electricity Industry Reform Amendment Bill was referred to the Committee on 11 December 2007. The closing date for submissions was 29 February 2008. We received and considered 22 submissions from interested groups and individuals. We heard 10 submissions. We received advice from the Ministry of Economic Development.

Committee membership

Gerry Brownlee (Chairperson)
Gordon Copeland (Deputy Chairperson)
Dave Hereora
Hon Darren Hughes (until 2 April 2008)
Hon Luamanuvao Winnie Laban
Simon Power
Hon Mita Ririnui (from 2 April 2008)
Hon Paul Swain
Lindsay Tisch
Dr Richard Worth

Electricity Industry Reform Amendment Bill

Key to symbols used in reprinted bill

As reported from a select committee

text inserted unanimously

~~text deleted unanimously~~

Hon David Parker

Electricity Industry Reform Amendment Bill

Government Bill

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The Parliament of New Zealand enacts as follows:

1 Title
This Act is the Electricity Industry Reform Amendment Act **2007**.

2 Commencement 5
This Act comes into force on the 28th day after the date on which it receives the Royal assent.

Part 1
Amendments to principal Act

3 Principal Act amended 10
This Part amends the Electricity Industry Reform Act 1998.

4 Purpose
(1) Section 2(1) is repealed and the following subsections are substituted:

“(1) The purpose of this Act is to better ensure ~~that~~— 15

“(a) that costs and prices in the electricity industry are subject to sustained downward pressure; and

“(b) that the benefits of efficient electricity pricing flow through to all classes of consumers; and

“(c) ~~barriers to~~ new investment in generation from renewable energy sources ~~are limited~~. 20

“(1A) The Act does this by—

“(a) effectively separating electricity lines from generation and retail where those activities are co-located; and

- “(b) promoting effective competition in electricity generation and retail; and
- “(c) limiting barriers to new investment in generation from renewable energy sources.”
- (2) Section 2(2) is repealed and the following subsection substituted: 5
- “(2) The particular purpose of Parts 1 to 3 and 5 (separation of lines and supply) is—
- “(a) to prohibit certain involvements in electricity lines and electricity generation and retail that may create incentives or opportunities— 10
- “(i) to inhibit competition in the electricity industry; or
- “(ii) to cross-subsidise generation or retail activities from electricity lines activities; and 15
- “(b) to restrict relationships between ~~businesses that have involvements in electricity lines and electricity generation or retail that otherwise may not be at arm’s-length~~ a business that has involvement in electricity lines and a business that has involvement in electricity generation or retail, where those relationships may not otherwise be at arm’s-length; and 20
- “(c) to provide specified exemptions for new investment in generation from renewable energy sources.”
- (2A) Section 2(4) is repealed. 25
- (3) Section 2(5) is repealed.

5 Interpretation

- (1) The definitions of **core assets, cross-involvement, customer co-operative, distributed generation, electricity business, electricity company, electricity lines business, electricity supply business, exempt person, existing cross-involvement, existing involvement, line, manager, mirror co-operative, mirror trust, nameplate, ownership separation rules, settling trust, transfer, and unseparated electricity business** in section 3(1) are repealed. 30 35
- (2) Section 3(1) is amended by inserting the following definitions in their appropriate alphabetical order:

“**connected customer**, in respect of a person, means a consumer (within the meaning of ~~that term in~~ section 2(1) of the Electricity Act 1992) to whom that person sells electricity, if—

“(a) the electricity is conveyed to that ~~customer~~ consumer on a line in which the person is involved; and

“(b) the ~~customer~~ consumer and the line are within the same local network area

“**connected customers selling cap** means the rule in **section 17C**

“**connected electricity business** means a business to which ~~section 17D~~ section 17D applies ~~has the same meaning as in section 17D~~

“**connected generation**, in respect of a person, means generation in which the person is involved that is connected to a line in which the person is involved, if the generation and the line are within the same local network area

“**connected generation cap** means the rule in **section 17A**

“**electricity business** means a business that does any of the things referred to in **section 7(1)(a) to (c)**

“**financial year** means a period of 12 months ending on 31 March

“**line** means works that are used or intended to be used for the conveyance of electricity, and includes a wire or cable

“**local network** means ~~lines, equipment, and plant that is used to convey electricity between the grid and a consumer or embedded generator or embedded network who are connected to that local network, and local network area has a corresponding meaning~~

“**local network** means the lines, and associated equipment, owned or operated by an electricity distributor (within the meaning of section 2(1) of the Electricity Act 1992) in a contiguous geographic area or areas but does not include the national grid, and local network area has a corresponding meaning

“**manager**, in relation to a person,—

“(a) means a person who, whether alone or jointly with any other person, manages, or directs or supervises the management of, the whole or a substantial part of the business and affairs of the person; and

- “(b) includes, for the avoidance of doubt,—
 “(i) in relation to a trust, a trustee:
 “(ii) in relation to a local authority, a member; but
 “(c) does not include,—
 “(i) in relation to a body corporate, a director of that 5
body corporate:
 “(ii) in relation to an electricity business in which a
local authority or any other person has an interest,
a member of that local authority or manager of
that person only as a result of having that position 10
- “**nameplate** means the full-load continuous rating of a gener-
ator under specific conditions as designated by its manufac-
turer and measured in megawatts in accordance with Inter-
national Electrotechnical Commission Standard 60034-1 or
any successor to that standard or any recognised equivalent 15
standard
- “**ownership separation rules** means the rules in **sections 17**
to 47F 17C and section 20 (non-specific interests rule)
- “**qualifying generation** has the same meaning as in **section**
17C(2) 20
- “**renewable energy source** means solar, wind, hydro, geother-
 mal, biomass, tidal, wave, ocean current sources, or any other
 energy source that occurs naturally and the use of which will
 not permanently deplete New Zealand’s energy sources of that
 kind, because those sources are generally expected to be re- 25
 plenished by natural processes within 50 years or less of being
 used
- “**sell** means any arrangement under which electricity is bought
 and sold, except financial hedge contracts, and **sell electricity**
 has a corresponding meaning”. 30
- (3) Every reference in the principal Act to “arms length rules” is
~~replaced~~ substituted by a reference to “arm’s-length rules”.
- (4) Section 3(3) is amended by omitting “sections 4(2), 5(2), and
 19” and substituting “**sections 17 to 47F** and 19”.
- 6 Sections 4 and 5 repealed** 35
 Sections 4 and 5 are repealed.

7 New sections 6 and 7 to 7A substituted

Sections 6 and 7 are repealed and the following sections substituted:

“6 Meaning of business A and business B

“(1) Where section 20 uses the term business A, it refers to a business that would have to ~~be~~ have its ownership separated under **sections 17 to 17F**, and the term business B then refers to a business from which business A must be separated under those sections. 5

“(2) Where the rest of this Act uses the term business A, it refers to a business that is required to be carried out in 1 company under **sections 17D and section 17E**, and the term business B then refers to a business that is required to be carried out in another company under ~~those sections~~ that section. 10

“(3) Where this Act applies to business A, it applies equally to business B, and vice versa. 15

“(4) References to trust A and trust B have corresponding meanings and application.

“7 Meaning of involved

“(1) For the purposes of this Act, a person is **involved**— 20

“(a) in a line if the person conveys electricity by the line, or owns or operates, directly or indirectly, the line or any other assets used in connection with the line, either alone or together with its associates and either on its own or another’s behalf: 25

“(b) in any generation if the person generates electricity from the generator, or owns or operates, directly or indirectly, the generator or any other assets used in connection with the generator, either alone or together with its associates and either on its own or another’s behalf: 30

“(c) in selling electricity to a customer if the person sells to the customer either on its own or another’s behalf:

“(d) in any of the things referred to in **paragraphs (a) to (c)** if the person— 35

“(i) carries on a business that does any of those things, either alone or together with its associates and either on its own or another’s behalf; or

- “(ii) exceeds the 10% threshold in section 8 in respect of a business that does any of those things; or
- “(iii) has material influence over a business that does any of those things.
- “(2) **Involvement** has a corresponding meaning. 5
- 7A** **How to measure involvement**
- “(1) This section applies for the purposes of calculating the caps and thresholds referred to in the following sections:
- “(a) **section 17A** (connected generation cap):
- “(b) **section 17C** (connected customers selling cap): 10
- “(c) **section 17D** (threshold for corporate separation and arm’s-length rules).
- “(2) A person is involved in any connected generation only in proportion to the extent of the person’s interest in the connected generation. 15

Examples

LineCo has a 20% shareholding in a joint venture company that operates a connected 100 MW generating plant.

LineCo is therefore involved in 20 MW of generation. Consequently, 20 MW of generation counts towards the cap on connected generation (50 MW in the case of thermal generation and unlimited in the case of renewable generation). 20

LineCo can sell to connected customers all of the total annual nominal MWh capacity of the 20 MW. The selling cap does not change in proportion to the extent of LineCo’s interest in the business selling the electricity. For example, if the business selling the electricity is a joint venture company in which LineCo has only a 30% shareholding, then LineCo’s selling cap is the same as it would have been if LineCo had a 100% shareholding in the selling business. 25

Fred is a director of LineCo. That directorship is his only interest in anything. Fred’s involvement in respect of both generation and selling is the same as LineCo’s. 30

LineCo must corporately separate and operate the generation and retail businesses at arm’s-length (because the 20 MW exceeds the 10 MW threshold). However, it does not need to have separate managers because the 20 MW does not exceed the 30 MW threshold for separate managers in the arm’s-length rules. 35

7A Meaning of material influence

(1) Section 11(1)(a) is amended by omitting “a manager” and substituting “a director or manager”.

(2) Section 11(2) is amended by omitting “its managers” and substituting “its directors or managers”.

5

7B Meaning of associate

Section 12(1) is amended by inserting the following paragraph after paragraph (d):

“(da) person A is a limited partnership or an overseas limited partnership and person B is a general partner or a limited partner who takes part in the management of the limited partnership (within the meaning of the Limited Partnerships Act 2008); or”

10

8 New headings and sections 17 to 17F substituted

Section 17 and the heading above section 17 are repealed and the following sections and headings substituted:

15

“Ownership separation

“17 Ownership restrictions on connected electricity businesses

“(1) No person who breaches the connected generation cap may be involved in the relevant line, and vice versa.

20

“(2) No person who breaches the connected customers selling cap may be involved in the relevant line, and vice versa.

“17 Ownership restrictions

“(1) The purpose of this section is to prevent a person being involved both in a line, and in generation or supply, in certain circumstances.

25

“(2) It is a contravention of this Part if a person has an involvement that is a breach of either or both of the following:

“(a) the connected generation cap:

“(b) the connected customers selling cap.

30

“Connected generation and connected
customers selling caps

“17A Connected generation cap rule

- “(1) The connected generation cap is breached by a person if—
- “(a) any of the person’s connected generation with a capacity greater than 5 MW in total (determined according to nameplate or nameplates) was commissioned before 20 May 2003; or
 - “(b) the person’s connected generation has a total capacity (determined according to nameplate or nameplates) that exceeds the greater of—
 - “(i) 50 MW; or
 - “(ii) 20% of the average of the maximum demand, in the immediately preceding 3 financial years, on the local network area.
- “(2) ~~Generation where the total capacity (determined according to nameplate or nameplates) of the generator is 5 MW or less is counted for the purpose of this section (regardless of when it was commissioned) unless it falls within **section 17B(c)**:~~
- “(3) This section is subject to **section 17B**.

“17B Small or encouraged connected generation not counted for purpose of connected generation cap

The following connected generation is not counted for the purpose of **section 17A** (but is counted for the purposes of **section 17D**, which relates to the threshold for corporate separation and arm’s-length rules):

- “(a) generation commissioned on or after 8 August 2001 if the electricity generated from it is produced only from renewable energy sources:
- “(b) generation commissioned on or after 8 August 2001 if the electricity generated from it is produced partly from renewable energy sources, as long as fossil fuels provide no more of the total fuel energy input for the generator or generators comprising the generation plant in any 12-month period than—
 - “(i) 20%; or
 - “(ii) any larger amount approved by the Minister (on the conditions, if any, he or she thinks fit) after

first taking into account whether or not the generation uses new or advanced technology:

- “(c) generation where the total capacity (determined according to nameplate or nameplates) of the generator is 5 MW or less if the generation was owned or operated, directly or indirectly, by the relevant person—
- “(i) before 23 June 1998; and
- “(ii) continuously between that date and the date when the person ~~seeks to count~~ counts that generation for the purposes of **section 17A**;
- “(d) generation that is disregarded under section 19.

“17C Connected customers selling cap rule

- “(1) The connected customers selling cap is breached by a person if the person is involved in selling more electricity to connected customers within a local network area, in total, in a financial year, than the equivalent of the person’s qualifying generation within the local network area.
- “(2) The person’s **qualifying generation** is the sum of the total annual nominal MWh capacity of the following generation (calculated as if the generation were operated at total capacity (determined according to nameplate or nameplates) for 24 hours for 365 days per annum):

$$a + b + c$$

where—

- a is the person’s connected generation that is ~~within~~ counted for the purpose of the connected generation cap in **section 17A**; and
- b is any connected generation referred to in **section 17B(a), (b), or (c)** in which the person has an involvement; and
- c is any ~~new~~ generation referred to in **section 17B(a) or (b)** that is connected to the national grid, if,—
- (a) on application by or on behalf of the person, the Commission has determined, by notice in the *Gazette*, that the generation should be treated as being within the local network area of the lines in which the person is involved; and

- (b) the total capacity (determined according to nameplate or nameplates) of all generation in which the person has an involvement does not exceed 100 MW.

“(3) The Commission may not determine that any generation should be treated as being within more than 1 local network area. 5

“Corporate separation and arm’s-length rules

“17D When corporate separation and arm’s-length rules apply

The corporate separation and arm’s-length rules apply if a person has an involvement in— 10

- “(a) more than 10 MW (determined according to nameplate or nameplates) of connected generation (including any connected generation referred to in **section 17B** and any generation that the Commission has determined under **section 17C(2)** should be treated as being within the local network area); or 15
- “(b) selling more than 87 600 MWh (which is 10 MW operated at 24 hours for 365 days per annum) of qualifying generation to connected customers in a financial year. 20

“17D Threshold for corporate separation and arm’s-length rules

A business is a **connected electricity business** if the business, or a person involved in the business, has an involvement in more than 10 MW (determined according to nameplate or nameplates) of connected generation (including any connected generation referred to in **section 17B** and any generation that the Commission has determined under **section 17C(2)** should be treated as being within a local network area). 25

“17E What Corporate separation and arm’s-length rules require imposed 30

“(1) The corporate separation rules require that Every person or persons who carry on the connected electricity businesses a connected electricity business must carry on the business involving the relevant line in a different company from the com- 35

pany that carries on the business involving the qualifying generation or the selling to connected customers.

- “(2) ~~The arm’s-length rules require that~~ Every person who is involved in either of the connected electricity businesses must comply, and ensure that the person’s electricity businesses 5 comply, with the arm’s-length rules.

“Use-of-systems agreements rules for businesses with 5 MW or more of connected generation

“17EA Use-of-systems agreements rules for businesses with 5 MW or more of connected generation 10

“(1) This section applies to an electricity business—

“(a) that either—

“(i) is required to comply with the arm’s-length rules;
or

“(ii) would be required to comply with the arm’s-length rules if the threshold for those rules were set at 5 MW of connected generation (instead of 10 MW); and 15

“(b) that sells more than 5 GWh of electricity to connected customers in a financial year. 20

“(2) Every director of that electricity business must ensure that—

“(a) the business has a comprehensive, written use-of-systems agreement that provides for the supply of line services (to the extent that those services are for the purpose of retailing) to the business that is involved in selling electricity (entered into, in the case of a business to which the corporate separation rule does not apply, as if the businesses were separate legal persons); and 25

“(b) the terms of that use-of-systems agreement do not discriminate in favour of one business and do not contain arrangements that include elements that the business usually omits, or omit elements that the business usually includes, in use-of-systems agreements with parties that are— 30

“(i) connected or related only by the transaction or dealing in question; and 35

“(ii) acting independently; and

“(iii) each acting in its own best interests; and

- “(c) the business operates in accordance with that use-of-systems agreement; and
- “(d) the business publishes that use-of-systems agreement on an Internet site maintained by or on behalf of the business so that it is available to the public at all reasonable times. 5
- “(3) The directors of that electricity business must publish on an Internet site maintained by or on behalf of the business, so that it is available to the public at all reasonable times, a certificate, signed by those directors, stating whether or not, in the preceding calendar year,— 10
- “(a) the terms in the use-of-systems agreement are a true and fair view of the terms on which line services were supplied in respect of the sales to which the agreement relates during that year; and 15
- “(b) **section 17EA** was otherwise fully complied with during that year.
- “(4) Every director commits an offence who—
- “(a) refuses or knowingly fails to comply with this section; or 20
- “(b) publishes a use-of-systems agreement or a certificate knowing that it is false or misleading in a material particular.
- “(5) Every director who commits an offence under **subsection (4)** is liable on summary conviction to a fine not exceeding \$200,000. 25

“Exemption for Transpower

- “17F **Exemption for Transpower New Zealand Limited for purpose of deferring investment in national grid**
- “(1) In this section, unless the context otherwise requires, **Transpower** means Transpower New Zealand Limited and any subsidiary of or successor to that company. 30
- “(2) This section applies if, and to the extent to which, Transpower contracts with another person for that person to generate electricity for the purpose of deferring the need for investment by Transpower in the national grid. 35

“(3) Transpower is not involved in that person’s electricity generation for the purposes of this Act.”

9 Section 18 repealed

Section 18 is repealed.

10 New heading above section 19 substituted

5

The heading above section 19 is repealed and the following heading substituted:

“Scope of application of rules in this Part”.

11 Certain businesses and involvements to be disregarded

(1) Section 19(1) is amended by inserting the following paragraphs after paragraph (ga):

“(gb) that person is involved in the generation of reserve energy that is in accordance with the terms and conditions for that reserve energy set by the Commission, as those terms are defined in the Electricity Act 1992; or

15

“(gc) that person is involved in the generation of electricity that is solely for the person’s own consumption or for the consumption of that person’s associates; or

“(gd) that person is involved in the generation of electricity that does not have a total annual nominal capacity greater than ~~2.5~~ 5 GWh per annum (determined according to nameplate or nameplates); or

20

“(ge) that person is involved in selling no more than 5 GWh of electricity to connected customers within a local network area, in total, in a financial year; or”

25

(2) Section 19 is amended by inserting the following subsection after subsection (1):

“(1A) For the purposes of this Act, no account is to be taken of a person’s involvement in a line that—

“(a) is not connected, directly or indirectly, to the national grid:

30

“(b) conveys electricity only from a generator to the national grid or from the national grid to a generator:

“(c) conveys less than ~~2.5~~ 5 GWh per annum:

- “(d) conveys electricity solely for the consumption of a person who is involved in the line or for the consumption of its associates:
- “(e) conveys electricity (other than via the national grid) only from a generator to a local network or from a local network to a generator: 5
- “(f) conveys electricity mostly in competition with another line or lines operated by another electricity business that is not an associate of a person who is involved in the first line, provided that the competition is actual competition and not potential competition.” 10

12 Sections 22 to 46C and headings repealed

Sections 22 to 46C and the headings above sections 22, 27, 28, 30, 31, 36, 37, 46, 46A, and 46C are repealed.

13 Inadvertent contraventions 15

- (1) Section ~~48~~ 48(1) is amended by omitting “(except for sections 25 and 36)”.
- (2) Section 48 is amended by adding the following subsection:
- “(3) This section does not apply to a contravention of **section 17D or 17E** (corporate separation and arm’s-length rules) or **section 17EA** (use-of-systems agreements).” 20

14 Court may order divestiture of assets or voting securities

Section 54 is amended by adding the following subsection:

- “(4) This section does not apply to a contravention of **section 17D or 17E** (corporate separation and arm’s-length rules) or **section 17EA** (use-of-systems agreements).” 25

15 Application of Commerce Act 1986 and Crown Entities Act 2004 provisions

Section 58 is amended by inserting the following paragraph after paragraph (c): 30

- “(ca) section 88A (when undertaking as to damages not required by Commission):”.

- 16 Part 4 repealed**
Part 4 (which relates to separation of lines and supply—taxation) is repealed.
- 17 Disclosure regime**
Section 70(1)(c) is repealed. 5
- 18 New sections 70A and 70B inserted**
The following sections are inserted after section 70:
- “70A Disclosure as to electricity sold to connected customers within local network area**
- “(1) Every person who sells electricity to connected customers must provide to the Commission, as soon as practicable after the end of each financial year, a statement that— 10
- “(a) shows the calculation of the person’s qualifying generation in respect of that financial year; and
- “(b) sets out how much electricity the person sold to connected customers during that financial year; and 15
- “(c) includes a certificate, signed by the directors of the electricity business, ~~confirming that~~ stating whether or not the quantity of electricity the person sold to connected customers during that financial year ~~did not exceed~~ exceeded the limit set out in **section 17C**. 20
- “(2) The statement must be in the form prescribed by the Commission from time to time.
- “(3) The statement must be audited by an independent chartered accountant. 25
- “(4) The statement must be published on an Internet ~~website~~ site maintained by or on behalf of the electricity business so that it is available to the public at all reasonable times.
- ~~“(5) Every person commits an offence who refuses or knowingly fails to provide the statement to the Commission.~~ 30
- “(5) Every person commits an offence who—
- “(a) refuses or knowingly fails to provide the statement to the Commission; or
- “(b) provides the statement to the Commission knowing that it is false or misleading in a material particular. 35

“(6) Every person who commits an offence under **subsection (5)** is liable on summary conviction to a fine not exceeding \$200,000.

“70B Directors must report compliance with arm’s-length rules

“(1) Each director of a business to which the arm’s-length rules apply must provide to the Commission, no later than 31 March in each year, a statement confirming whether or not the director has complied with all of the arm’s-length rules during the preceding calendar year. 5

“(2) The director must publish that statement on an Internet ~~website~~ site maintained by or on behalf of the business so that it is available to the public at all reasonable times.” 10

19 Sections 71 to 79 and heading above section 71 repealed

Sections 71 to 79 and the heading above section 71 are repealed. 15

20 Not interconnected under Commerce Act 1986

Section 83 is amended by omitting “an electricity lines business and an electricity supply business that do not have ownership separation” and substituting “businesses to which **sections 17D and 17E** (corporate separation and arm’s-length rules) apply”. 20

21 Sections 84 and 85 repealed

Sections 84 and 85 are repealed.

22 Regulations

(1) Section 87(2)(a), (c), and (d) are repealed. 25

(2) Section 87(2)(f) is amended by omitting “electricity lines businesses and electricity supply”.

22A Part 7 repealed

Part 7 (which contains amendments to the Electricity Act 1992) is repealed. 30

23 Part 8 repealed

Part 8 (which relates to the split of the Electricity Corporation of New Zealand) is repealed.

24 Schedule 1 amended

(1) Clause 1 of Schedule 1 is amended by repealing subclause (1) 5
and substituting the following subclause:

“(1) The objective of this schedule is to ensure that businesses referred to in **section 17D** operate at arm’s-length.”

(2) Clause 2 of Schedule 1 is amended by repealing the heading above rule 7 and rules 7 to 9 and substituting the following 10
headings and rules:

“At least 1 independent director

“7 At least 1 director of business A must—

“(a) be neither a director nor a manager of business B; and

“(b) not be an associate of business B, other than by virtue 15
of being a director of business A.

“No cross-directors who are executive directors

“8 A director of business A may be a director of business B, but must not—

“(a) manage business B on a day-to-day basis; or 20

“(b) be an associate of business B, other than by virtue of being a director of business A or business B; or

“(c) be involved in business B (other than by having material influence over business B by virtue of being a director of business B). 25

“Separate management rule

“9 (1) This clause applies if business A is involved in—

“(a) more than 30 MW (determined according to nameplate or nameplates) of connected generation (including any connected generation referred to in **section 17B** and 30
any generation that the Commission has determined

- under **section 47C(2)** should be treated as being within the local network area); or
- “(b) selling more than 262 800 MWh (which is 30 MW operated at 24 hours for 365 days per annum) of qualifying generation to connected customers. 5
- “(2) A manager of business A must not—
- “(a) be a manager of business B; or
- “(b) be an associate of business B, other than by virtue of being a manager of business A; or
- “(c) be involved in the business of business B.” 10
- (3) Clause 2 of Schedule 1 is amended by inserting the heading “*Managers must not be placed under certain obligations*” above rule 10(1).
- (4) Rule 10(2) of clause 2 of Schedule 1 is amended by inserting “; or a cross-director or a cross-manager,” after “common parent”. 15
- (5) Rule 11 of clause 2 of Schedule 1 is amended by adding the following subclauses as subclauses (2) and (3):
- “(2) This rule does not prevent cross-directors under **rule 8** from having access to normal board information. 20
- “(3) A manager of business A who is not prohibited from being a manager of business B under **rule 9** may use restricted information of both business A and business B, but only to the extent that the use does not contravene another of the arm’s-length rules.” 25
- (6) Clause 5 of Schedule 1 is repealed.

24 Schedule 1 substituted

Schedule 1 is repealed and the Schedule 1 set out in the Schedule of this Act substituted.

Part 2

30

Amendments to other Acts and transitional provision

25 Consequential amendments to Commerce Act 1986

- (1) This section and **section 26** amend the Commerce Act 1986.

- (2) The definitions of **electricity business**, **electricity lines business**, and **involved** in section 57D(1) are repealed.
- (3) Section 57D is amended by adding the following subsections:
- “(3) In this Part, unless the context otherwise requires,—
- “**electricity business** means an electricity lines business or an electricity supply business or an unseparated electricity business 5
- “**electricity lines business** has the same meaning as in **section 57DAA**
- “**electricity supply business** has the same meaning as in **section 57DAAB** 10
- “**involved** has the same meaning as it did in section 7 of the Electricity Industry Reform Act 1998 before the enactment of the **Electricity Industry Reform Amendment Act 2008**.
- “(4) In relation to **sections 57DAA and 57DAAB**,— 15
- “(a) limitations, exclusions, or exemptions under those sections may be applied cumulatively; and
- “(b) references to an activity being carried out only or solely for a particular purpose or in a particular way must not be read as excluding reliance on any other limitation, exclusion, or exemption in either of those sections.” 20
- 26 New sections 57DAA and 57DAAB inserted**
- The following sections are inserted after section 57D:
- “**57DAA Meaning of electricity lines business**
- “(1) For the purposes of this Part, **electricity lines business**— 25
- “(a) means a business that conveys electricity by line in New Zealand; and
- “(b) includes the ownership or operation, directly or indirectly, of lines in New Zealand or any other core assets of an electricity lines business. 30
- “(2) None of the following activities brings a person within **subsection (1)**:
- “(a) conveying, together with its associates (if any), less than 2.5 GWh per annum:
- “(b) conveying electricity solely for its own consumption or for the consumption of its associates: 35

- “(c) conveying electricity only from a generator to the national grid or from the national grid to a generator:
- “(d) conveying electricity (other than via the national grid) only from a generator to a local distribution network or from a local distribution network to a generator: 5
- “(e) conveying electricity by lines that are owned or operated by a business that also owns or operates a generator which generates electricity solely for the consumption of a local community, where both those lines and that generator are not connected, directly or indirectly, to the national grid: 10
- “(f) conveying electricity only by a line or lines that are mostly in competition with a line or lines operated by another electricity lines business that is not an associate of the person, provided that the competition is actual competition and not potential competition: 15
- “(g) owning or operating, directly or indirectly, lines referred to in any of **paragraphs (a) to (f)** or any other core assets of an electricity lines business used in connection with those lines. 20
- “(3) Terms used in this definition have the same meanings as they did in the Electricity Industry Reform Act 1998 before the enactment of the **Electricity Industry Reform Amendment Act 2007**.
- “**57DAAB Meaning of electricity supply business** 25
- “(1) For the purposes of this Part, **electricity supply business**—
- “(a) means a business that—
- “(i) sells electricity in New Zealand:
- “(ii) sells financial hedges for risks relating to the price of electricity in New Zealand: 30
- “(iii) generates electricity in New Zealand:
- “(iv) trades in rights to sell or generate electricity in New Zealand; and
- “(b) includes the ownership or operation, directly or indirectly, of a generator in New Zealand or any other core generation assets; and 35

- “(c) includes the ownership or operation, directly or indirectly, of any core assets of an electricity retail business, which include—
- “(i) the customer database relating to, and used for the purposes of, an electricity retail or electricity trading business; and 5
 - “(ii) the benefit of a contract to sell electricity; and
 - “(iii) the benefit of an undertaking from any other electricity supply business not to compete with the business. 10
- “(2) None of the following activities brings a person within **subsection (1)**:
- “(a) ~~selling or~~ generating or selling less than 2.5 GWh per annum: 15
 - “(b) generating or selling electricity solely for its own consumption or for the consumption of its associates: 15
 - “(c) generating electricity solely for the consumption of a local community, where—
 - “(i) the generator is owned or operated by a business that also conveys electricity by line; and 20
 - “(ii) both those lines and that generator are not connected, directly or indirectly, to the national grid: 20
 - “(d) selling electricity that is generated at a generator referred to in **paragraph (c)** or **subsection (3)**: 25
 - “(e) generating electricity from distributed generation, and selling the electricity generated, ~~where~~ if—
 - “(i) the generating capacity of the distributed generation is no more, at any one time, than the greater of 5 MW (determined according to nameplate or nameplates) and 2% of the maximum demand, in the immediately preceding financial year, of the lines to which the distributed generation is connected; and 30
 - “(ii) the distributed generation is owned or operated by a business that also conveys electricity by line and that distributed generation is connected to those lines: 35

- “(f) selling financial transmission rights that hedge risks arising from the effects of losses and constraints on the national grid:
- “(g) owning or operating, directly or indirectly, a generator referred to in any of **paragraphs (b) to (f)** or **subsection (3)** or any other core generation assets used in connection with those generators. 5
- “(3) A person may, without coming within **subsection (1)**, generate electricity at a generator or generators that are existing, and capable of generating electricity, as at 23 June 1998, if the total generating capacity (determined according to nameplate or nameplates) of the business, together with its associates (if any), is 5 MW or less. 10
- “(4) Transpower New Zealand Limited, and any subsidiary of or successor to that company, may, without coming within **subsection (1)**, contract with an electricity supply business for that electricity supply business to generate electricity for the purpose of deferring the need for investment by Transpower New Zealand Limited, or any subsidiary of or successor to that company, in the national grid. 15 20
- “(5) For the purposes of **subsection (2)**,—
- “**financial transmission right** means a financial instrument issued by the real time co-ordinator of electricity supply and demand in New Zealand that—
- “(a) is funded exclusively by the difference between purchaser payments and generator receipts on the sale and purchase of electricity in the wholesale market that arises from the effect of losses and constraints on the national grid; and 25
- “(b) entitles the holder to receive, or requires the holder to make, payments in accordance with a formula based on prices for quantities of electricity at 1 or more points on the national grid 30
- “**financial year** means a period of 12 months ending on 31 March 35
- “**system** means all of the works over which a business conveys or intends to convey electricity.

“(6) Other terms used in this definition have the same meanings as they did in the Electricity Industry Reform Act 1998 before the enactment of the **Electricity Industry Reform Amendment Act 2007**.”

27 Consequential amendment to Electricity Act 1992 5

(1) This section amends the Electricity Act 1992.

(2) Section 4A is amended by repealing subsection (1) and substituting the following subsection:

“(1) The Minister may, by notice in the *Gazette*, declare an electricity generator to be an electricity operator for the purposes of this Act, or any provision or provisions of this Act, if the Minister is satisfied—

“(a) that the declaration is necessary to enable the person to commence or carry on an activity as an electricity generator; and

“(b) that the business interests in respect of which the declaration is made are confined to any or all of the works necessary to convey the electricity generated to an electricity installation owned by an electricity generator, electricity distributor, or a consumer.”

28 Saving of existing exemptions

(1) This section applies to any exemption granted under section 81 of the Electricity Industry Reform Act 1998 in respect of a cross-involvement if the cross-involvement would continue to be unlawful after the enactment of this Act but for the exemption.

(2) The exemption, and the conditions subject to which it was granted, continue to have effect in so far as they apply to the cross-involvement as if this Act had not been enacted.

Schedule**s 24****New Schedule 1 substituted****Schedule 1****s 3(1) 5****Arm's-length rules****1 Objective**

- (1) The objective of this schedule is to ensure that connected electricity businesses operate at arm's-length.
- (2) Without limiting the ordinary meaning of the expression, arm's-length includes having relationships, dealings, and transactions that—
 - (a) do not include elements that parties in their respective positions would usually omit; or
 - (b) do not omit elements that parties in their respective positions would usually include,—
if the parties were—
 - (c) connected or related only by the transaction or dealing in question; and
 - (d) acting independently; and
 - (e) each acting in its own best interests.

2 Arm's-length rules

The arm's-length rules are as follows:

Duty to ensure arm's-length objective is met

1. Business A and every parent of business A, and business B and every parent of business B, must take all reasonable steps to ensure that the arm's-length objective in clause 1 is met.

Arm's-length test

2. Business A, and every parent of business A, must not enter into a transaction in which business B, or any parent of business B, is interested if the terms of the transaction are terms which unrelated parties in the position of the parties to the transaction, each acting independently and in its own best interests, would not have agreed to.

Duty not to prefer interests of business B

3. A director or manager of business A must not, when exercising powers or performing duties in connection with business A, act in a manner that the director or manager knows or ought reasonably to know would prefer the interests of business B over the interests of business A.

Schedule 1—*continued**Duty not to discriminate in favour of business B*

4. Business A must not, in providing services or benefits, discriminate in favour of business B or the customers, suppliers, or members of business B.

Duty to focus on interests of right ultimate owners

5. A director or manager of business A must, when exercising powers or performing duties in connection with business A, act in the interests of the ultimate members of business A in their capacity as such, and must neither subordinate the interests of those members to the interests of the members of business B nor, to the extent that the members or ultimate beneficial members of each business overlap, take account of that fact or have regard to their dual capacity as members of business B and business A.

Duty of directors and managers of parents of business A

6. A director or manager of a parent of business A must not, when exercising powers or performing duties in connection with business A, act in a manner that the director or manager knows or ought reasonably to know would prefer the interests of business B, or of the customers, suppliers, or members of business B in that capacity, over the interests of business A or the customers, suppliers, or members of business A.

At least 1 independent director

7. At least 1 director of business A must—
(a) be neither a director nor a manager of business B; and
(b) not be an associate of business B, other than by virtue of being a director of business A.

No cross-directors who are executive directors

8. A director of business A may be a director of business B, but must not—
(a) manage business B on a day-to-day basis; or
(b) be an associate of business B, other than by virtue of being a director of business A or business B; or
(c) be involved in business B (other than by having material influence over business B by virtue of being a director of business B).

Schedule 1—*continued**Separate management rule*

9. (1) This clause applies if business A is involved in more than 30 MW (determined according to nameplate or nameplates) of connected generation (including any connected generation referred to in **section 17B** and any generation that the Commission has determined under **section 17C(2)**) should be treated as being within the local network area.
- (2) A manager of business A must not—
- (a) be a manager of business B; or
 - (b) be an associate of business B, other than by virtue of being a manager of business A; or
 - (c) be involved in the business of business B.

Directors and managers must not be placed under certain obligations

10. (1) Subject to subclause (2), no person may place the director or manager of business A under an obligation, whether enforceable or not, to act in accordance with the directions, instructions, or wishes of business B, or any director or manager or associate of business B, or any parent of business B, and no director or manager may submit to any such obligation.
- (2) A common parent, or a cross-director or a cross-manager, of both business A and business B may place a director or manager under such an obligation if doing so does not contravene another of the arm's-length rules.

Restriction on use of information

11. (1) Business A must not disclose or permit the disclosure to business B, or use or permit the use for the purposes of business B, of restricted information of business A.
- An electricity trust that is a parent of business A (**trust A**), business A, and every parent of trust A, must not disclose or permit the disclosure to business B, an electricity trust that is a parent of business B (**trust B**), or any parent of trust B, or use or permit the use for the purposes of business B or trust B, of restricted information of business A or trust A.
- In these rules, **restricted information** is information received or generated, and held, by business A or trust A connected with its business, being information which—
- (a) is not available to the competitors or potential competitors of business B or trust B; and
 - (b) if disclosed to business B or trust B, would put, or be likely to put, business B or trust B in a position of material advantage in relation to any competitor or potential competitor.

Schedule 1—*continued*

- (2) This rule does not prevent cross-directors under **rule 8** from having access to normal board information.
- (3) A manager of business A who is not prohibited from being a manager of business B under **rule 9** may use restricted information of both business A and business B, but only to the extent that the use does not contravene another of the arm's-length rules.

Records

12. Every business to which this schedule applies must keep at its registered office a register of transactions entered into between business A, or any parent of business A, and business B, or any parent of business B.
13. Business A must, within 10 working days of entering into any such transaction, enter in its register details sufficient to identify the nature and import of the transaction.

Practical considerations

14. Business A and every parent of business A must ensure that its practical arrangements, such as use of accommodation, equipment, and services, do not contravene this schedule.
15. Business A and every parent of business A must ensure that its selection and appointment of advisors does not prejudice compliance with rules 7 to 11.

3 Rules do not limit objective

The arm's-length rules in clause 2 do not limit the generality of the arm's-length objective in clause 1.

4 Interpretation

- (1) In this schedule,— 5
- (a) **common parent**, in relation to business A and business B, means a person that is involved in both business A and business B:
- (b) **parent**, in relation to a business, means every person that is involved in the business. 10
- (2) In this schedule, a person is **interested** in a transaction if the person, or an associate of that person,—
- (a) is a party to, or will derive a material financial benefit from, the transaction; or
- (b) has a material financial interest in a party to the transaction; or 15

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Schedule 1—*continued*

- (c) is a director or manager of a party to, or a person who will or may derive a material financial benefit from, the transaction; or
- (d) is otherwise directly or indirectly materially interested in the transaction. 5
- (3) References in this schedule to business A or trust A apply equally to business B or trust B and vice versa.
- 5** **These duties are additional to other duties**
The requirements of this schedule are additional to the requirements of any regulations made under the Electricity Act 1992. 10

Legislative history

4 December 2007	Introduction (Bill 191–1)
11 December 2007	First reading and referral to Commerce Committee
