

14 September 2020

Jason Woolley, Sam Fleming
Meridian Energy Limited
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By email

Dear Jason, Sam,

1. You have asked us to review the submissions made to the Electricity Authority in response to its Preliminary Decision on a claim of an undesirable trading situation dated 30 June 2020 ("**Preliminary Decision**").
2. As part of that review, we have identified the following areas of concern:
 - (a) Some submitters invite the Authority to take into account irrelevant considerations. As Meridian identified in its submission, the Authority is undertaking a quasi-judicial function when investigating a UTS. It can only consider information that is probative of whether a UTS occurred.
 - (b) The Authority has misinterpreted the effect of clause 5.1A of the Electricity Industry Participation Code 2010 ("**Code**") in the Preliminary Decision. That misinterpretation, however, did not impact the Preliminary Decision as the Authority only considered a UTS to have occurred within the ten working day time limit. Other submitters, however, now seek to extend that preliminary UTS outside the time limit. The Authority cannot lawfully do so.
 - (c) The complainants submit that the Authority should consider allegations of a breach of the Commerce Act 1986. The Authority can consider breaches of the law.¹ The submission, however, fundamentally misconceives the law in question.

Relevant and irrelevant considerations

3. In undertaking a UTS investigation, the Authority is acting as an adjudicative body. It must answer the specific question before it, did a UTS arise, without

¹ Code, cl 5.1(2)(c).

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consideration of factors that are not probative of anything that determines that question.

Environmental considerations

4. Genesis and other submitters suggest the Authority should consider environmental impacts of the conduct in question in determining whether a UTS occurred.² They do not, however, explain how those considerations could have any impact on confidence in, or the integrity of, the wholesale market. We are of the view that environmental impacts of market actions are an irrelevant consideration in a UTS investigation.
5. A UTS investigation considers whether the confidence in, or integrity of, the wholesale market is or may be threatened. In considering that test, the Authority acts as a judicial decision-maker. It cannot further its strategic ambition in relation to kaitiaki and environmental concerns through application of its judicial function in UTS investigations.³
6. There is simply no plausible link between CO₂ being emitted and wholesale market confidence or integrity. Accordingly, environmental concerns cannot be a relevant consideration in determining a UTS investigation. It appears that the Authority, correctly, did not consider these concerns in its Preliminary Decision, notwithstanding their inclusion in the initial complaint.⁴ Any change to that approach in the Authority's final decision would amount to it wrongly taking into account an irrelevant consideration.

Purpose

7. Haast, OJI + Independent retailers' ("**complainants**") submit that the purpose of Meridian's actions are relevant to the UTS investigation. Specifically, that Meridian's alleged purpose to avoid transmission constraints binding is relevant to a UTS investigation.⁵ Again, there is no explained link between the purported purpose of Meridian's actions (which, even if it were accurate, would only amount to an allegation of normal market conduct) and the test for a UTS.
8. As the Authority has noted previously, a UTS is a notorious event that will be noticed quickly by market participants.⁶ Such a situation must be sufficient to impact the confidence in, or integrity of, the wholesale market. A participant's purpose could be relevant to whether such a situation occurred (for instance in relation to the examples in cl 5.1(2)). A participant's purpose for, say, entering hedges might be relevant if it was being done because of a loss of confidence in

² See *Haast, OJI + Independent retailers' UTS preliminary decision submission* at 22-23; *Genesis UTS preliminary decision submission* at [48]–[57].

³ *Haast, OJI + Independent retailers' UTS preliminary decision submission* at 22.

⁴ Preliminary Decision at [4.2(f)].

⁵ *Haast, OJI + Independent retailers' UTS preliminary decision submission* at 21.

⁶ Electricity Authority *Decision Paper: Review of the Undesirable Trading Situation Provisions in the Code* at [4.7.4]–[4.7.5].

the market. However, the Authority can only consider the purpose of a participant's actions if, and to the extent, it is demonstrated to be relevant to the test for a UTS. The complainants have failed to do so here.

Limitation period

9. The Authority misinterpreted cl 5.1A of the Code. Properly construed, cl 5.1A precludes a finding of a UTS at any time prior to the 10 business days immediately preceding the commencement of the Authority's investigation of a UTS.
10. Clause 5.1A provides that the "Authority must not commence an investigation if more than 10 business days have passed since the situation, which the Authority suspects or anticipates may be an undesirable trading situation, occurred."
11. The Authority considered cl 5.1A had "no other effect" than impacting when the Authority may *begin* a UTS investigation.⁷ The Authority began an investigation on 13 December 2020, having received a complaint on 12 December 2020. It considered that cl 5.1A had therefore been satisfied and the clause had no further impact on the timeframe of activity it could consider as it started an investigation within 10 business days of receiving the complaint.⁸ Crucial to this interpretation was the ongoing nature of the UTS alleged. The complainants rely on this reasoning to submit that a UTS occurred from 10 November 2019 until 16 January 2020.
12. The proper interpretation of cl 5.1A, however, precludes the Authority from finding a UTS "occurred" any earlier than ten working days prior to the commencement of the Authority's investigation.
13. The Authority's interpretation in its Preliminary Decision allows perverse outcomes. On the Authority's approach, provided the complainant alleges an ongoing situation, the Authority is licensed to retrospectively investigate that situation, however historical it may in fact be. In this way, how a claimant frames their allegation determines the jurisdiction of the Authority. That cannot be right.
14. The Authority's interpretation also involved an unduly literal reading of cl 5.1A. In applying that reading it failed to take into account the purpose and context of the rule, as it was required to do.⁹
15. The purpose of a rule can be informed by its history. Clause 5.1A was proposed in its present form by the Authority.¹⁰ The Authority's views on the proposal at inception support the limitation period's operation as (at a minimum) a time limit

⁷ Preliminary Decision at [9.2].

⁸ Preliminary Decision at [9.3].

⁹ See Interpretation Act 1999, s 5; and *Commerce Commission v Fonterra Co-operative Group Ltd* [2007] 3 NZLR 767, [2007] NZSC 36 at [22].

¹⁰ Electricity Authority *Consultation Paper: Review of the Undesirable Trading Situation Provisions in the Code*.

between the relevant events capable of supporting a UTS finding and the commencement of the Authority's investigation. Indeed, in its strongest form, the Authority's own view of its limitation period could be read as precluding *any* investigation once 10 business days have passed from the *commencement* of a UTS (which, if the complainants are correct as to the 10 November commencement of the UTS, would in fact prevent *any* investigation by the Authority in this case):¹¹

... the Authority considers that it is more appropriate for the time limit on initiating a UTS investigation to start from the date that an alleged UTS commenced. This would mean that the UTS provisions could not be triggered if a UTS was first discovered after the time limit expired. While a scenario of this type cannot entirely be ruled out, it appears very unlikely that a situation which threatens or may threaten confidence in, or the integrity of, the wholesale market, could go unnoticed for a long period.

16. The Authority further explained that a short limitation period was appropriate in the context that "any situation that meets the test of being a UTS is extremely unlikely to go unnoticed for any extended period".¹² All prior UTS allegations had been lodged within "hours or days of the relevant triggering contingency or event".¹³ Such quick reaction is consistent with a market that prices in 30 minute windows.
17. A short limitation period (and correspondingly short period capable of investigation/finding of a UTS) is also consistent with the purpose of the UTS regime as a whole, which is to urgently restore proper market operation.¹⁴
18. A short limitation period is also consistent with the High Court's view that a UTS will typically be "one off" events of relatively short duration" because longer running situations are unlikely to be properly conceived of as a UTS.¹⁵ Such long running situations would be appropriate for the Code change process, as the Authority recognised in its Decision Paper:¹⁶

the UTS provisions should not be relied upon as a fix-all in place of Code amendments. The Authority expects that any situation that has gone unnoticed for a sustained period is likely to be more appropriately handled by amending the Code on a prospective basis

¹¹ At [3.1.39] see also [3.1.42]–[3.1.43].

¹² At 3.1.42.

¹³ At 3.1.42.

¹⁴ See cl 5.5.

¹⁵ *Bay of Plenty Energy Limited v the Electricity Authority* HC Wellington CIV-2011-485-1371, 27 February 2012 at [218].

¹⁶ Electricity Authority *Decision Paper: Review of the Undesirable Trading Situation Provisions in the Code* at [4.6.4](c).

19. The proper interpretation is that once an investigation is launched, the Authority can only consider whether a UTS "occurred" in the immediately preceding ten business days. If the alleged UTS is alleged to have begun earlier than those ten business days, the Authority cannot make findings of a UTS in respect of that prior period.
20. This interpretation of the Code, which is consistent with the purpose and context of the UTS regime, is also supported by the relevant jurisprudence in respect of the limitation provision in s 80(5) of the Commerce Act, which is framed in a materially identical way. There, conduct that "arose" more than three years ago (where the limitation period was three years) has been held not to be capable of being the subject of Commerce Commission proceedings, notwithstanding a situation where the ongoing conduct had continued so that some of it occurred within the three year limitation period.¹⁷ Only the conduct falling within the limitation period was potentially prosecutable, despite the ongoing conduct itself spanning both before and after the three year cut-off.
21. For all the above reasons, the Authority's view that cl 5.1A had "no other effect" than limiting when it might "*begin* an investigation" is wrong.¹⁸
22. Accordingly, submitters are wrong to seek to expand the time period for consideration of whether a UTS occurred before the ten business day period immediately preceding the commencement of the Authority's investigation. The limitation period precludes findings of a UTS for those earlier periods.

No misuse of market power

23. The complainants' submission suggests that the Authority's investigation could be "supported and strengthened" by considering whether Meridian had misused its market power, with that apparent breach of s 36 of the Commerce Act used to evidence a UTS.¹⁹ As the Authority is aware, the Commerce Act is enforced by the Commerce Commission not the Electricity Authority. It is not clear how an allegation of misuse of market power is in any way relevant to whether confidence in, or the integrity of, the wholesale market has been threatened.
24. The complainants' submission exhibits a fundamental misunderstanding of the scheme of the Commerce Act, and its relationship to the Code. For example, the complainants' submission confuses the statutory tests for the cartel prohibitions (which, contrary to the complainants' submission, are not concerned with any lessening of competition) and s 36 (which, contrary to the complainants' submission, is not a purpose and effects test, but solely considers the defendant's purpose).²⁰

¹⁷ *Commerce Commission v Koppers Arch Wood Protection (NZ) Ltd* [2007] 2 NZLR 805 (HC) at [58]–[59].

¹⁸ Preliminary Decision at 9.2 (emphasis in original).

¹⁹ Haast, OJI + Independent retailers' UTS preliminary decision submission at 21.

²⁰ At 21.

25. Whether Meridian has market power and, if so, whether it "misused it" in December 2019, is a separate question to whether confidence in, or the integrity of, the wholesale market has been threatened. However, for the avoidance of doubt, there is no reasonable basis on which to assert that Meridian's conduct breaches s 36 of the Commerce Act:
- (a) s 36 only applies to businesses with a "substantial degree of market power". The Commission has previously found that the wholesale market should be defined on a national basis.²¹ Meridian faces vigorous competition from Mercury, Genesis, Contact, Trustpower and a number of others in that national market, and was not acting "substantially unconstrained by competitive pressures"²² during December 2019;
 - (b) the prohibition requires a "taking advantage" of a substantial degree of market power for an anticompetitive purpose. The Courts have found that "taking advantage" means that if Meridian could have engaged in identical conduct if it did not have market power, there is no breach of s 36.²³ The fact that two other generators (Genesis and Contact) were independently engaged in similar conduct in response to unprecedented conditions in the lower South Island, is in and of itself evidence that Meridian's conduct did not constitute a "taking advantage" of any alleged market power; and
 - (c) Meridian was not acting with any of the proscribed purposes listed in s 36(2) of the Commerce Act. As set out in Meridian's submission in response to the Authority's preliminary decision, the purpose of Meridian's conduct in December 2019 was to manage the entirely unprecedented level of rainfall safely, and mitigate the risks to communities, property, and structures in its catchments. Meridian's offers were within normal parameters of the market, and consistent with past analogous periods. Even if those prices exceeded the Authority's expectations they were not high, and in any event the Courts have previously recognised that an anti-competitive purpose cannot be inferred from high prices alone.²⁴

²¹ Investigation Report: Commerce Act 1986, s 27, s 30 and s 36 Electricity Investigation (22 May 2009).

²² *Commerce Commission v Telecom Corp New Zealand* [2010] NZSC 111, [2011] 1 NZLR 577 at [33].

²³ At [31].

²⁴ *Telecom Corp of New Zealand Ltd v Clear Communications Ltd* [1995] 1 NZLR 385 (PC) at 406–409.

26. We would be pleased to respond to any further questions Meridian may have in relation to the above advice.

Yours faithfully
RUSSELL McVEAGH

A handwritten signature in blue ink, appearing to be 'Chris Curran' or 'Sarah Keene', with a long horizontal stroke extending to the right.

Chris Curran | Sarah Keene
Partners