

BELL GULLY



Commercial Quarterly

SUMMER 2008



Welcome to the Summer 2008 issue of *Commercial Quarterly*, Bell Gully's digest of current corporate and commercial law issues.

Each quarter we preview upcoming developments and summarise recent cases, articles and legislation of interest under the following headings:

Commercial business law
Company law
Securities and capital markets
Competition and consumer law
Intellectual property and information technology
Utilities and resources

In this issue, feature articles include:

- an update on the latest changes made to the Limited Partnerships Bill;
- a discussion on the new Property Law Act and its impact on everyday commercial transactions;
- the effect of amalgamations on existing contracts with third parties;
- the latest Financial Reporting Act class exemptions;
- commentary on the new "truth in takeovers" provisions;
- Bell Gully's responses to the Takeovers Panel's reform of the Companies Act reconstruction provisions;
- an outline of the final key securities law changes which come into effect on 29 February;
- commentary on the Commerce Commission's review of the internal merger clearance process;
- privacy in the online world;
- key issues to consider when choosing a business name;
- the latest developments in the electricity sector;
- a discussion on why efficiency thresholds will remain important for lines businesses; and
- key issues facing the forestry sector arising from the proposed climate change legislation.

Previous issues of Commercial Quarterly are available on our website.

A companion publication, *Regulator Report*, covers developments in the corporate and regulatory sector (New Zealand and Australian exchanges, securities markets regulators, and takeovers and competition regulators) and is published approximately every three weeks. *Regulator Report* is available online at www.bellgully.com.

Need more information? For more information on any of the cases, articles and features in *Commercial Quarterly*, please email Diane Graham at diane.graham@bellgully.com or call on 64 9 916 8849.

Disclaimer: This publication is necessarily brief and general in nature. You should seek professional advice before taking any action in relation to the matters dealt with in this publication.

Commercial business law

Limited Partnerships Bill – still room for improvement

Proposed changes to the Bill establishing limited partnerships in New Zealand will make the structure more appealing to investors but, as Bell Gully partner Andrew Abernethy points out in this article, there are still some key issues to be sorted.

New Property Law Act – impacts on everyday commercial transactions

On 1 January 2008 the new Property Law Act came into force, bringing the law of real property into the 21st century. The new Property Law Act, like its predecessor, does not just deal with real property transactions, it contains rules of general law relating to the creation, disposition and control of property of all kinds. In this article we look at changes made to some of the more general statutory rules governing deeds and other instruments.

Commercial business law

Limited Partnerships Bill – still room for improvement

Proposed changes to the Bill establishing limited partnerships in New Zealand will make the structure more appealing to investors but, as Bell Gully partner Andrew Abernethy points out in this article, there are still some key issues to be sorted.

In December 2007 the Commerce Select Committee reported back to Parliament on the Limited Partnerships Bill introduced in August to establish a new regulatory and tax regime for New Zealand for limited partnerships - the internationally preferred legal structure for investing in venture capital.

The Commerce Select Committee's key changes

The committee has recommended several changes which improve the attractiveness of New Zealand limited partnerships as an alternative investment vehicle. Key changes include:

Contracting out obligations

The fiduciary obligations of a general partner to the limited partners may now be contracted out of through the relevant Limited Partnership agreement. A new clause also provides that a limited partner does not have any fiduciary obligations to the limited partnership or to any other partner. While fiduciary principles may have their place in contractual dealings, they are not ideal as mandatory principles for participants in limited partnerships. It is encouraging to see that these principles are now "default" rules, which may be contracted out of by relevant partners. The overseas experience has been that mandatory inclusion of fiduciary principles into a structure such as the limited partnership creates operational uncertainties and inefficiencies.

Information disclosure

The select committee has also proposed a change in requirements around the provision of limited partnership information. While certain information regarding limited partners must be provided to the Registrar of Companies, it is now not to be made available to members of the public (and is not to be subject to Official Information Act requests). The disclosure of limited partnership information, in some jurisdictions, goes beyond basic information and into details of capital commitments. Given that limited partners are not responsible for the debts of the partnership, other than for unpaid capital, details of the identity of the partners rarely provides useful information to members of the public (and is often sensitive).

Business restrictions

Restrictions on limited partnerships engaging in banking and insurance or on listing on securities markets have been deleted from the Bill. The place for these restrictions is in industry-specific regulation (such as banking and insurance legislation or in stock exchange listing rules) rather than an entity-type regulation. There is nothing in the nature of a limited partnership that makes it more or less suitable for listing on the stock exchange, for example, than any other sort of entity.

Remaining areas for improvement

While the amendments are an improvement, there are still several areas where the Bill could be significantly improved.

Control rule

The so-called "control rule", which provides that limited partners are responsible for the debts of the limited partnership if they engage in "control type" activities, is not a good idea even when it is coupled, as anticipated, with a long list of authorised "safe harbour" activities. The Commerce Committee has recommended only that the list of safe harbours be moved from regulations to be made under the Act into the body of the Act itself.

The "control rule" creates uncertainty around limited partners exercising veto, voting and other control rights over the management and operation of the limited partnership and therefore requires elaborate and often exhaustive lists of permitted activities. The rule has led, in its application, to uncertainty and costs for market participants in the administration of limited partnerships worldwide.

A better approach has been adopted by the National Conference of Commissioners on Uniform State Laws in the United States. It does away with the control rule altogether and provides that limited partners are not liable for the obligations of the partnership even if they do engage in the management and control of the limited partnership. The National Conference of Commissioners adopted this principle because it believed that the control rule had become an anachronism in a world with limited partnerships, limited liability companies and other flow through entities and that eliminating the control rule would allow for the "next logical step in the evolution of the limited partnership".

In its submission, Bell Gully recommended that the draft Bill be amended to remove the control rule and with it the need to draft (and continue to keep updated in line with international jurisdictions) the list of safe harbours.

Limited partnership agreement

The Bill has moved from requiring that limited partnerships have a limited partnership agreement to requiring that the limited partnership agreement itself covers certain specified matters. To save time, litigation costs and uncertainty for participants, it would be preferable to create a default set of rules that apply in the absence of agreement to the contrary.

Given the sophisticated nature of participants who are likely to use limited partnerships, almost all limited partnerships established will have detailed limited partnership agreements. Even so, we do not consider that it is good use of public funds to have courts dealing with situations in which the partners to a limited partnership have not addressed a matter that could have been dealt with in default rules.

Taxation of capital gains

One of the principal benefits of limited partnership structures internationally is the ability to compensate the general partner through its "carried interest" profit participation. A key element of this is that the character of the partnership gains (i.e., capital gains or ordinary income) are preserved in the hands of all partners (whether limited partners or general partners). In theory, this allows a general partner to receive a "performance fee" as a non-taxable capital gain (and on which no value added or sales tax) would be assessable.

However, under New Zealand income tax law partnership gains derived from realisations of portfolio securities will, where those securities are held on revenue account, be taxed at marginal income tax rates, to all partners – thereby making the structure less attractive in some respects than a "portfolio investment entity" which pays no tax on sales of New Zealand (and some Australian) equity securities.

Next steps

The Bill is currently awaiting its second reading in Parliament. If it passes into law as planned, the Bill will come into force on 1 April 2008. In the meantime, regulations (provided for in the Bill) will need to be enacted before the Bill comes into force. We will keep you informed of any further developments.

For further information on the Bill contact [Andrew Abernethy](#) or your usual Bell Gully adviser.

To access a copy of the Select Committee's Report on the Limited Partnerships Bill visit Parliament's website www.parliament.nz or [click here](#).

To access a copy of the consultation document for the Limited Partnerships Bill: Safe Harbours and Fees Regulations visit the Ministry of Economic Development's website www.med.govt.nz or [click here](#)

Commercial business law

New Property Law Act – impacts on everyday commercial transactions

On 1 January 2008 the new Property Law Act came into force, bringing the law of real property into the 21st century. The new Property Law Act, like its predecessor, does not just deal with real property transactions, it contains rules of general law relating to the creation, disposition and control of property of all kinds. In this article we look at changes made to some of the more general statutory rules governing deeds and other instruments.

The Property Law Act 2007 (the Act) came into effect on 1 January 2008. The Act repealed the Property Law Act 1952 and the Contracts Enforcement Act 1956.

The Act is primarily focussed on property law issues and should help provide certainty in property dealings; facilitate the resolution of disputes; and reduce litigation for property owners, landlords and tenants. For more information on these aspects of the Act refer to the article "*New Property Law Act creates positive reforms*" in Bell Gully's recent [Property Update](#). Bell Gully has also published an article on how the Act impacts on financiers, especially in relation to the restrictions and enforcements of loans secured by a mortgage. To view this article [click here](#).

In addition to the specific property law provisions, the Act also establishes a new set of general statutory rules governing deeds and other instruments. These aspects are summarised briefly below.

Formalities required for deeds

It is a matter of everyday, practical importance that the way an individual, a company or other corporation executes a binding document should be well-known, simple and rational.

This is especially important for the more formal requirements of the law governing deeds. It is therefore unfortunate that the overhaul of the statutory rules governing deeds in part 2 of the Act raises a new uncertainty over the requirements for "delivery" of a deed.

Delivery of deeds

The new wording in section 9 of the Act prescribes that a deed must be in writing, executed and delivered in accordance with the terms of that section. The Act states that delivery can be effected by the person to be bound by the deed or by another person who has express or implied authority to deliver it on behalf of the person intended to be bound by it.

The draft legislation proposed by the Law Commission stated that it would be sufficient to constitute "delivery" if:

- it was apparent from the circumstances that the person to be bound by the deed intended to be bound by it or,
- if the binding force of the deed was subject to the fulfilment of one or more conditions, each of those conditions had been fulfilled.

This therefore precluded the need for "formal" or "literal" delivery as provided for in the old section 4 of the 1952 Act.

Although the same language proposed by the Law Commission has been adopted in section 9(9)(a) of the Act, it does not appear to be included as an explanation of what constitutes delivery, which is how it was originally intended. Instead, it appears to read as an additional requirement to the delivery obligation. We hope that this is an unintentional drafting error which will be rectified by the legislature in due course.

In any event, with the addition of the new statutory requirement for delivery, we would recommend that warranties and confirmations regarding due execution of a deed be extended to provide confirmation that the deed has also been delivered.

Execution of deeds

The Act sets out the requirements for how a body corporate, the Crown, an individual and an attorney may enter into a deed.

(a) Bodies corporate

A body corporate may still enter into a deed in the manner prescribed by another statute. Therefore, a company registered under the Companies Act 1993 may also enter into a deed in the manner provided in section 180(1)(a) of that Act, although the provisions of the Act in relation to execution of a deed by a body corporate are generally consistent with section 180(1)(a) of the Companies Act.

Under section 9(3) of the Act, a body corporate must execute a deed through the signature of:

- o a single director (if the body corporate has only one director);
- o not fewer than two directors (if the body corporate has two or more directors);
- o one director or another person or member of a specified class of person if the body corporate's constitution authorises a deed to be signed in that way.

Except where a deed is executed by two or more directors, the signature of the signatory to the deed must be witnessed.

A body corporate which is incorporated outside New Zealand may also execute a deed in the manner permitted under the law of the place in which the body corporate is incorporated, were the deed executed in that place and governed by that law.

(b) Crown

One or more Ministers of the Crown may execute a deed on behalf of the Crown, but where a deed is executed by only one Minister it must also be witnessed.

(c) Individual

An individual must execute a deed by signing the deed and having their signature witnessed.

(d) Attorney

An attorney may execute a deed, although they must be appointed by deed.

Attestation of deeds

A person witnessing execution of a deed must not be a party to the deed. The witness must sign the deed and, if the deed is signed in New Zealand, the witness must add the name of the city, town or locality where they ordinarily reside and their occupation or description. No particular form of words is required for the description of the address or occupation of a witness.

Execution of other contracts by bodies corporate

The Act also sets out how a New Zealand incorporated company may enter into any other contract or obligation and those requirements reflect the provisions of section 180(1)(b) and (c) of the Companies Act 1993.

Those rules will also apply to non-New Zealand companies in relation to any contract or other obligation entered into in New Zealand or any contract or other obligation for which the proper law is the law of New Zealand (subject to any law of the place in which the company is incorporated).

Execution of instruments by an attorney

An instrument executed by an attorney must be made in the name of the donor, state that it is being executed on the donor's behalf by the donor's attorney, and otherwise be executed by the attorney in the same manner as would be required if the attorney were a party to the instrument.

Certificates of non-revocation of power of attorney

Under the Property Law Act 1952 a certificate of non-revocation of power of attorney could be in the form scheduled to that Act "or to like effect".

The Act requires a certificate of non-revocation of power of attorney to be in the form set out in schedule 1 to the Act. There is no provision for any variation from that form. The certificate must be signed by the attorney or, if the attorney is a body corporate, a director or other officer of the body corporate or a person acting on behalf of the body corporate in another capacity.

The Act also prescribes when the certificate must be given. It must be given immediately before, or at any time after, the doing of a thing by the attorney.

Specific performance of voluntary promises made by deed

In common law, a person wishing to enforce a voluntary promise (a promise made without consideration) made by a deed could only claim damages and could not seek specific performance of the promise. This rule is changed by section 18 of the Act so that courts are now able to order specific performance of a voluntary promise made by a deed.

Material alterations to a deed

Section 11 of the Act abolishes the old rule that a deed becomes invalid if there is a material alteration after its execution.

Changes for assignments of things in action

Sections 48 to 53 of the Act introduce a number of changes to the law governing assignment of things in action including:

- provision for the assignment of part of a debt to operate as a legal assignment by the extension of the definition of a "thing in action" to include a "part of a thing in action";
- clarification of the position in relation to the assignment of specified future debts;
- confirmation that consideration is not required to effect a valid legal assignment of a thing of action;
- changes to the requirements to give notice for a statutory assignment of a thing in action;
- clarification for an assignor's agent to execute an instrument of assignment; and
- a new regime setting out the requirements for the valid equitable assignment of a thing in action.

To access the new Property Law Act 2007 online visit the Government's legislation website www.legislation.govt.nz or [click here](#).

For further information or advice on the new Property Law Act please contact your usual Bell Gully adviser.

Company law

Amalgamations and their effect on existing contractual arrangements

In this case note Bell Gully partner Jayne Kirton and solicitor Neetha Alex review a recent Court of Appeal decision dealing with the legal consequences on third party contracts of court ordered amalgamations under Part 15 of the Companies Act. The case also illustrates how important it is for contracting parties to consider their requirements in the event there is a change of control through an amalgamation and to ensure that those requirements are included in the contract.

Financial Reporting Act Class Exemptions for Australian and United States incorporated companies

In 2006 a new power was given to the Registrar of Companies to exempt certain overseas companies from compliance with various provisions of the Financial Reporting Act as part of the Government's programme to improve the workability of the financial reporting system and reduce business compliance. In this note Bell Gully partner Glenn Joblin and solicitor Ryan Ellis provide an overview of the two class exemptions issued by the Registrar of Companies since the new provisions came into effect.

Company law

Amalgamations and their effect on existing contractual arrangements

In this case note Bell Gully partner Jayne Kirton and solicitor Neetha Alex review a recent Court of Appeal decision dealing with the legal consequences on third party contracts of court ordered amalgamations under Part 15 of the Companies Act. The case also illustrates how important it is for contracting parties to consider their requirements in the event there is a change of control through an amalgamation and to ensure that those requirements are included in the contract.

Since the decision in *Carter Holt Harvey Ltd v McKernan*,¹ it has been established in New Zealand that the effect of an amalgamation implemented under Part 13 of the Companies Act 1993 (the Act) is that the amalgamated company stands “in the shoes of the amalgamating companies” and therefore receives the benefits of, and incurs the obligations pertaining to, all assets and liabilities of the amalgamating companies.

The amalgamation does not result in each amalgamating company transferring its rights in assets and liabilities to the amalgamated company while the former entities continue to exist as part of the latter, post-amalgamation.

The amalgamated company is not treated as a different party for the purposes of third party contractual arrangements. In a recent decision, *Elders New Zealand Ltd v PGG Wrightson Ltd*,² the Court of Appeal upheld the High Court’s earlier decision that court ordered amalgamations under Part 15 of the Act could result in the same legal consequences as amalgamations under Part 13 of the Act, outlined above.

The background facts

Wrightson and Elders (and in some cases, their associated companies) were co-owners of a number of stock saleyards. The parties’ rights in respect of such saleyards were regulated by either agreements or the constitutions of the co-owned companies, all of which provided for rights of pre-emption in the event that any one of the co-owners sought to “...transfer...or otherwise dispose of the whole or part of its interest in...” the relevant stockyard.

Wrightson entered into a scheme of arrangement with Pyne Gould Guinness under Part 15 of the Act whereby Wrightson would amalgamate into Pyne Gould Guinness (to be renamed PGG Wrightson Limited post-amalgamation). The High Court granted final orders, approving the arrangement. Elders then issued proceedings seeking a declaration that the arrangement triggered Elders’ pre-emptive rights in the co-owned companies.

The High Court found in favour of PGG Wrightson on the basis that the court approved amalgamation procedure under Part 15 of the Act had the same effect as an amalgamation effected under Part 13 - that is the amalgamated company stands “in the shoes of the amalgamating companies” .

Following *Carter Holt Harvey Ltd v McKernan*³ therefore, there was no transfer of Wrightson’s interest in the co-owned saleyards to PGG Wrightson, as was required to trigger any right of pre-emption held by Elders. Elders appealed to the Court of Appeal.

The decision

The Court of Appeal found that Part 15 of the Act offers entities an alternate scheme to implement amalgamations and that once such approval is obtained, amalgamations under Part 15 of the Act have the same legal consequences as those effected under Part 13 of the Act.

¹ [1998] 3 NZLR 403

² [2007] NZCA 596

³ [1998] 3 NZLR 403

The court noted section 236(1) (being the primary operative section in Part 15 of the Act) does not define the role of the court with any clarity. Therefore some ambiguity is created. However it concluded that it would be untenable to interpret the court's jurisdiction under Part 15 of the Act as being confined to such amalgamations which have already been effected under Part 13 of the Act.

Factors the court considered in reaching its decision were:

- Although section 236(1) does not cast the court's role as one of approval, such language is expressly used in the heading for Part 15 of the Act and in various sections under that Part.
- Section 238 of the Act affirms an interpretation of Part 15 of the Act as offering an *additional* mechanism for implementing amalgamations which could otherwise have been effected under Part 13 of the Act.
- The court can therefore sanction an amalgamation even if all the requirements (particularly those relating to public advertising and minority buy-out rights) for amalgamations under Part 13 of the Act have not been met.

Although the court accepted that the final orders granted by the High Court approving the amalgamation were only expressed to be binding on Wrightson, Pyne Gould Guinness and their shareholders, the court considered it inappropriate to argue that such orders were not also binding on Elders.

Because the merger plan specified the effects of the amalgamation in a way which correlated to the effects of an amalgamation under Part 13 - stating that PGG Wrightson would "...succeed to all the property, right, powers and privileges...[and] all liabilities and obligations of Wrightson..." - the court concluded that an amalgamation in the Part 13 sense had been effected.

In that context, the court found that PGG Wrightson was to be treated as the same party as Wrightson for the purposes of the latter's business dealings with Elders. There had therefore been no transfer to PGG Wrightson of Wrightson's interests in the relevant stockyards. In the absence of such transfer, and given that the terms of the rights of pre-emption contained in the relevant agreements and constitutions were triggered only by a *transfer or disposal* of the relevant interests, the court dismissed Elders' appeal.

Practical implications

Parties to a commercial relationship should take care when drafting the terms of pre-emptive rights and change of control provisions. As noted by the court in this case, the particular facts gave rise to a change of control. The amalgamation would therefore have invoked Elders' rights of pre-emption had those rights been expressed to be triggered by such change of control.

Change of control issues (particularly in relation to joint ventures and non-competition clauses) should be carefully considered and any trigger clause appropriately worded to ensure that it applies in a manner that suits the parties' requirements in the event that counterparties are involved in an amalgamation. Providing for these considerations will maximise the benefit a party derives from such provisions.

Company law

Financial Reporting Act Class Exemptions for Australian and United States incorporated companies

In 2006 a new power was given to the Registrar of Companies to exempt certain overseas companies from compliance with various provisions of the Financial Reporting Act as part of the Government's programme to improve the workability of the financial reporting system and reduce business compliance. In this note Bell Gully partner Glenn Joblin and solicitor Ryan Ellis provide an overview of the two class exemptions issued by the Registrar of Companies since the new provisions came into effect.

Financial reporting obligations

Under the Financial Reporting Act 1993 (FRA), all overseas incorporated companies carrying on business in New Zealand are required to prepare financial statements that comply with the FRA. Those financial statements comprise:

- financial statements in respect of the entire activities of the overseas company;
- consolidated group financial statements (if the company has any subsidiaries); and
- financial statements solely in respect of the activities of the overseas company's New Zealand business.

The requirements under (a) and (b) above are often onerous as many overseas companies which are part of a group of companies are not required to prepare financial statements under the laws of the country in which they are incorporated.

Following the 2006 amendments to the FRA, the Registrar of Companies may exempt the directors of an overseas company from compliance with various provisions of the FRA. The Registrar cannot grant exemptions for any overseas company which is an "issuer" under the FRA (eg. listed entities), although an issuer may apply to the Securities Commission for an exemption under the FRA.

The Registrar of Companies has recently issued two class exemptions and a specific exemption for a particular entity.

Class exemptions

The following class exemptions have been issued:

- (a) the Financial Reporting Act (Overseas Incorporated Companies – United States of America) Exemption Notice 2007; and
- (b) the Financial Reporting Act (Overseas Incorporated Companies – Australian Wholly-Owned Entities) Exemption Notice 2007.

The effect of these class exemptions is that Australian and United States incorporated companies carrying on business in New Zealand may be exempted from certain financial reporting obligations under the FRA.

United States overseas companies class exemption

The effect of this class exemption is to allow overseas companies incorporated in the United States to provide the group financial statements that they are required to prepare under financial reporting requirements in the United States.

Overseas companies relying on the class exemption will be required to:

- prepare and register financial statements for their New Zealand business and consolidated financial statements only (not stand-alone company financial statements);
- ensure that the consolidated financial statements comply with generally accepted accounting principles in the United States (rather than generally accepted accounting practice in New Zealand); and

have those consolidated financial statements audited in accordance with the requirements set out in United States legislation and the auditor's report will provide the information required by United States legislation.

For United States incorporated companies to gain the benefit of the class exemption, the consolidated financial statements which are to be filed in New Zealand must be accompanied by a report by an approved auditor that complies with the requirements of Part 210 of the Code of Federal Regulations (US).

To access a copy of this class exemption visit the Government's legislation website www.legislation.govt.nz or [click here](#).

Australian overseas companies class exemption

The effect of this class exemption is to allow overseas companies incorporated in Australia, which are wholly-owned subsidiaries that have been granted relief under the Australian Securities and Investment Commission's Class Order [98/1418] Wholly-owned entities, to file consolidated financial statements for the parent entity only that are required to be prepared in accordance with the Class Order.

Exempted companies will not be required to prepare stand-alone financial statements, although they will remain obliged to prepare, and file with the Companies Office, financial statements for their New Zealand business.

The exemptions are subject to the following conditions:

the consolidated financial statements prepared in accordance with the Class Order must comply with generally accepted accounting principles in Australia and include any additional information and explanations that are necessary to ensure that those financial statements give a true and fair view of the matters to which they relate; and

the following documents must be delivered to the Companies Office:

- (i) a copy of those consolidated financial statements;
- (ii) a memorandum signed by the directors of the overseas company providing various confirmations relating to those consolidated financial statements and the relief granted under the Class Order; and
- (iii) a copy of the deed of cross guarantee entered into by the overseas company in accordance with the Class Order.

To access a copy of this class exemption visit the Government's legislation website www.legislation.govt.nz.

Securities and capital markets

Truth in takeovers: market participants should prepare for a more rigorous approach

The Takeovers Panel will have new powers to deal with misleading or deceptive conduct in relation to Takeovers Code-regulated transactions when the new provisions in the Takeovers Act and Rule 64 of the Takeovers Code come into force on 29 February. In this article partner Glenn Joblin and solicitor Tony Dunn review the new provisions and highlight what can be expected from the Takeovers Panel in light of its recent policy announcements on the new law.

Bell Gully responds to the latest Takeovers Panel's reform proposals for Schemes of Arrangement and Amalgamations involving Code Companies

In this article we outline the proposals put forward by the Takeovers Panel in its latest consultation paper on "Schemes of Arrangement and Amalgamations involving Code Companies" and explain why Bell Gully has advised against the addition of further protections.

Final changes arising from Securities Legislation Bill in force on 29 February

Regular readers of Commercial Quarterly will already be aware that the last of the changes made by the 2006 Securities Legislation Bill come into effect on 29 February. In this note we provide you with a brief outline of the final key components of the Government's securities reform package which are now in place.

Securities and capital markets

Truth in takeovers: market participants should prepare for a more rigorous approach

The Takeovers Panel will have new powers to deal with misleading or deceptive conduct in relation to Takeovers Code-regulated transactions when the new provisions in the Takeovers Act and Rule 64 of the Takeovers Code come into force on 29 February. In this article partner Glenn Joblin and solicitor Tony Dunn review the new provisions and highlight what can be expected from the Takeovers Panel in light of its recent policy announcements on the new law.

Background

The 2006 Securities Legislation Bill included a number of changes to the Takeovers Act and Takeovers Code. Most of these came into effect after the Bill's assent in October 2006. The most significant amendments to the Takeovers Act and the Takeovers Code to arise out of the Bill are new provisions which introduce market manipulation prohibitions in relation to takeovers. These amendments come into force on 29 February 2008.

The amendments are a direct response to the Takeovers Panel's calls to government for additional powers to respond to allegations of misleading conduct in relation to takeovers.

The new provisions, which in equivalent Australian legislation are commonly known as "truth in takeovers" provisions, are broad and will cover communications outside the formal offer document and target company statements, including newspaper advertising campaigns and letters sent to shareholders directly. The provisions will provide additional scope for those involved in hostile or contested takeovers to complain about the conduct of other parties.

The key changes are set out in section 44B of the Takeovers Act and Rule 64 of the Takeovers Code.

Section 44B

Under section 44B of the Takeovers Act a person must not make a statement or disseminate information in relation to any transaction or event regulated by the Takeovers Code if:

- a *material* aspect of the statement or information is false or the statement or information is materially misleading; *and*
- the statement or information is likely to:
 - induce a person to trade, or *hold* the securities; or
 - have the effect of increasing, reducing, maintaining or stabilising the price for trading of the securities; or
 - induce a person to vote for, vote against, or abstain from voting in respect of a transaction that is or is likely to be regulated by the Takeovers Code.

A person or company who contravenes section 44B can be held criminally liable if they have *actual knowledge* that the statement or information is false in a material aspect or is materially misleading.

Rule 64

The Takeovers Panel's ability to address misleading conduct has in the past been limited to situations where an offer document or target company statement is misleading. Rule 64 of the Takeovers Code extends the Takeovers Panel's jurisdiction to any conduct concerning a Takeovers Code-regulated transaction or event.

Under Rule 64, a person must not engage in conduct that is:

- conduct in relation to any transaction or event that is regulated by the Takeovers Code and misleading or deceptive or likely to mislead or deceive; or
- incidental or preliminary to a transaction or event that is or is likely to be regulated by the Takeovers Code and misleading or deceptive or likely to mislead or deceive.

In essence, Rule 64 has imported section 9 of the Fair Trading Act 1986 (which prohibits misleading and deceptive conduct in trade) into the Takeovers Code. As a consequence, the Fair Trading Act will not apply to conduct regulated by the Takeovers Code.

In most situations, complaints in relation to a breach of Rule 64 will relate to written or oral statements. However, Rule 64 relates to "conduct" and therefore not only to statements or representations. The Takeovers Panel may be able to regard conduct, such as trading in shares, as being misleading or deceptive in certain circumstances.

Rule 64 applies to conduct by any person, not just bidders or target companies or major shareholders.

Rule 64(2) allows the Takeovers Panel to take action in advance of Takeovers Code-regulated transactions or events. For example, the Takeovers Panel may require correcting information to be issued before a formal takeover offer is made or that a notice of meeting be changed before it is sent to shareholders.

Takeovers Panel's policy position on new law provided in Code Word 22

In preparation for the implementation of the new regime, the Takeovers Panel has provided some early clarification of its interpretation of, and its intended approach to, the new "truth in takeovers" provisions in issue 22 of its periodic publication, Code Word.

For the most part, the Takeovers Panel has drawn on the detailed policies developed by the Australian Takeovers Panel and the Australian Securities and Investments Commission in relation to Australia's truth in takeovers provisions. It has also drawn on New Zealand case law dealing with section 9 of the Fair Trading Act. Particular mention is made of:

- how the Takeovers Panel intends to construe the meaning of misleading or deceptive conduct;
- how the Takeovers Panel will deal with "last and final statements";
- the likely manner in which the Takeovers Panel will use its new enforcement powers; and
- how the Takeovers Panel intends to control the provisions being used by some as a tactical measure against their opponents.

Meaning of misleading or deceptive conduct

The Takeovers Panel has given some guidance as to how it will interpret the expression "misleading or deceptive". The Takeovers Panel has stated that its interpretation will be consistent with pronouncements of the New Zealand and Australian courts and it will consider Takeovers Code-regulated conduct to be "misleading" or "deceptive" if it leads, or will be likely to lead, a person into error.

Last and final statements

The parties to a takeover offer are often asked to comment on their intended actions, and in some cases, a bidder will make a statement that it will not increase the offer price or extend the offer period. These announcements, commonly referred to as "last and final statements", can influence the actions of the directors or shareholders of the target company. The Takeovers Panel has indicated that even statements of a party's present intentions may be regarded as "last and final statements." For example, a bidder who states that it has "no intention to increase its offer price" may be regarded by the Panel as having acted in a misleading and deceptive manner if it does subsequently increase its offer price. That interpretation is at odds with ordinary legal principles where a statement of present intention would not be considered misleading if it was the party's genuine intention at the time the statement was made.

A recent example of a regulator enforcing the "truth in takeovers" principles in relation to "last and final statements" is the Australian Takeover Panel's decision in relation to the successful Australian takeover offer of Rinker Group Limited by CEMEX.

During its takeover bid for Rinker, CEMEX made a public announcement on 10 April 2007 that its offer price at that point was its best and final offer in the absence of a superior proposal. On 7 May 2007

however, CEMEX announced that Rinker shareholders that accept the offer could retain a final dividend that had been announced by Rinker in the interim, effectively increasing the offer price per share.

The Australian Takeovers Panel found that CEMEX's 7 May announcement resiled from the 10 April announcement and therefore, in the time between the two announcements:

- the acquisition of Rinker shares did not take place in an efficient, competitive and informed market;
- Rinker shareholders and the market were entitled to assume that there would be no other improvements to the offer after 10 April;
- Rinker shareholders and the directors of Rinker were not given enough information to enable them to assess the merits of the offer; and
- Rinker shareholders who sold shares on market after the 10 April announcement and before the 7 May announcement did not have an equal opportunity to share in the benefits flowing from the offer (i.e., the effective increase in the offer arising from the dividend).

CEMEX was ordered to pay the amount of the final dividend per share to Rinker shareholders who sold their shares in the period between the two announcements.

A similar outcome could arise under New Zealand's new provisions. The Takeovers Panel has stated that a departure from an unqualified "last and final statement" is likely to be seen as misleading or deceptive conduct. Furthermore, the Takeovers Panel has stated that it intends to "rigorously enforce" the prohibition against misleading or deceptive conduct and the Takeovers Panel has new enforcement powers to carry this out.

The Takeovers Panel has stated that there is scope to preserve the right to depart from a "last and final statement" by making a clear and unequivocal qualification when the statement is made. The Takeovers Panel, in Code Word 22, considers that an example of a clearly qualified statement would be:

"At present [Offeror Ltd] does not intend to increase the offer price, but it reserves the right to do so."

The Takeovers Panel has stated that, as a matter of practice, it intends to write to each party who makes a "last and final statement" at the time of publication or when the statement is drawn to the Takeovers Panel's attention. The person will be put on notice that unqualified statements must be adhered to. If the statement is unqualified, the Takeovers Panel will ask whether an unqualified statement is what was really intended. If it was not intended to be an unqualified statement, the person will be invited to promptly publish a qualification to the statement. If the statement is equivocally qualified, the Takeovers Panel will invite the person to clarify their position to the market and to the Takeovers Panel immediately.

Enforcement provisions

Permanent compliance orders

The Takeovers Panel will be able to issue permanent compliance orders to deal with misleading conduct (section 33AA of the Takeovers Act).

Permanent compliance orders will enable the Takeovers Panel to prohibit or restrict persons from making statements or distributing documents, and to direct persons to disclose information or to publish, at the person's own expense, corrective statements. The power to grant permanent compliance orders will allow the Takeovers Panel to achieve by enforceable orders what it can often, but not always, accomplish with co-operation from the party who has breached the Takeovers Code.

The changes to the Takeovers Act also allow the Takeovers Panel to issue compliance orders in respect of any secondary involvement in a breach or contravention of the Takeovers Code (for example, against a person who has aided or abetted or induced any other person to contravene the Takeovers Code). Previously, the Takeovers Panel could only take action against the person or persons breaching the Takeovers Code.

Pecuniary penalties

The High Court can order civil remedies for a contravention of the Takeovers Code, including a compensatory order or pecuniary penalty order. The Takeovers Panel has indicated that it may apply to the Court for a pecuniary penalty order if a person is found to have deliberately misled or deceived

market participants. The maximum pecuniary penalty is \$500,000 for an individual or \$5,000,000 for a body corporate, for each contravention.

Takeovers Panel may apply threshold tests

The Takeovers Panel has identified the possibility that its resources may be wasted dealing with tactical or vexatious complaints in relation to misleading or deceptive conduct. It has noted in Code Word 22 that the Takeovers Panel may apply threshold tests to decide whether to act on a complaint about misleading or deceptive conduct. A complainant may be required to show that it has a prima facie case, or that the complaint is not vexatious, or establish that there would be sufficient merit in having the Takeovers Panel investigate their complaint.

A final warning – no intention required

Market participants will already be aware of the need to take care if they make any representations to the media or the market in relation to a takeover. However, this will be even more important when Rule 64 is operative.

No element of intention to mislead or deceive is required for conduct to be in breach of the Rule. Conduct that unintentionally leads a person into error may still be a breach of the Takeovers Code.

It is clear that market participants will need to closely scrutinise all media statements and other communications issued in relation to a takeover or other Takeovers Code-regulated transaction.

For full details of the Takeovers Panel's intended approach to the new law read Code Word 22 on the Panel's website www.takeovers.govt.nz or [click here](#)

Securities and capital markets

Bell Gully responds to the latest Takeovers Panel's reform proposals for Schemes of Arrangement and Amalgamations involving Code Companies

In this article we outline the proposals put forward by the Takeovers Panel in its latest consultation paper on "Schemes of Arrangement and Amalgamations involving Code Companies" and explain why Bell Gully has advised against the addition of further protections.

Background

In December 2007 the Takeovers Panel released a consultation paper to address its concerns (and those of some market participants) over the perceived trend for Code companies to use schemes of arrangement and amalgamations in order to circumvent the requirements of the Takeovers Code. The consultation paper follows the panel's June 2006 discussion paper on the same matter, and the panel's subsequent recommendations to the Minister of Commerce and to the Commerce Select Committee in which the panel called for legislative amendments to be included as part of the 2006 Business Law Reform Bill in order to address the problem. This request failed and in March 2007 the panel was asked by the Minister of Commerce to lead a further review and consultation process on this matter with market participants.

The 2007 Consultation Paper

The latest Takeovers Panel consultation paper has been prepared with the assistance of the New Zealand Institute of Economic Research (NZIER). The paper includes an overview of the current position relating to the regulation of changes of control applicable to Code companies and provides a comprehensive discussion on the panel's views of the problems arising from the use of the Companies Act reconstruction provisions (namely Part XIII, which deals with amalgamations, and Part XV, which deals with schemes of arrangements) to effect changes of control of Code companies.

The Takeovers Panel's chief concern centres on the process used by Code companies to achieve a change of control as it regards the Takeovers Code's procedures as prescribing a minimum standard for Code companies. In particular it notes that the requirements of the Takeovers Code are designed to be fairer, to provide equality of treatment and to give shareholders greater protection from the potential adverse consequences of a change in control. In contrast, the panel considers that the use of the reconstruction provisions in the Companies Act by Code companies to effect a change of control can give rise to an inferior process with negative effects on shareholders' rights.

According to the panel there are five principal alternatives to the option of maintaining the status quo. In brief:

- Option one involves the insertion of anti-avoidance provisions into the reconstruction provisions of the Companies Act along the lines of the position in Australia. This would include amendments being made to Part XV of the Companies Act to require the court to withhold approval for any scheme until it is satisfied that the scheme has not been proposed to avoid the Code, or unless the panel has provided a "no-objection" statement. A similar "no-objection" statement could also be a prerequisite for an amalgamation under Part XIII.
- Option two involves an amendment of the Takeovers Act and the Code to exempt schemes and amalgamations involving Code companies from the Code, while amending the Companies Act to ensure the panel has a greater involvement in the reconstruction process as set out in option one.
- Option three involves an amendment of the reconstruction provisions of the Companies Act so that shareholder approval thresholds and shareholder information requirements are consistent with those in the Code. Although it is recognised that in making this alignment there are issues over the degree of shareholder approval necessary and over the coverage of which shareholders should be entitled to vote.
- Option four involves an amendment of the reconstruction provisions of the Companies Act so that amalgamations under Part XIII of the Companies Act cannot be undertaken if a Code company is involved. As schemes would still be available where Code companies are involved, this option could be implemented in conjunction with either option one or option three in respect of schemes.

- Option five which would involve an amendment of the reconstruction provisions of the Companies Act so that neither amalgamations or schemes of arrangements could be used where Code companies were involved, except with the permission of the panel in circumstances where the use of the reconstruction provisions is clearly warranted.

The panel notes in the paper that it is approaching the issue of reform in this area with an open mind and that the options outlined in the paper are to generate discussion and to assist in reaching conclusions on the way forward. This is in marked contrast to the panel's earlier attempts to address this issue in 2006 when the panel was clearly in favour of a similar approach to that outlined in option two, whereby the provisions in the Takeovers Code for schemes and amalgamations would be removed from the Code and instead be incorporated as part of the Companies Act provisions in Parts XIII and XV of the Act. In particular the panel recommended in its 2006 submissions to the Minister of Commerce that:

- Part XIII of the Companies Act be amended to require that:
 - parties to a proposed amalgamation must obtain the approval of the panel to the amalgamation process; and
 - the panel, in giving approval for an amalgamation process, shall take into account the principles of the Takeovers Code; and
- Part XV of the Companies Act be amended to require that:
 - the courts take into account the principles of the Takeovers Code when deciding the requirements for approval of a scheme of arrangement, including the level of shareholder approval required and the information to be provided to shareholders; and
 - before approving a scheme of arrangement the court receives and takes into account recommendations from the panel as to the requirements to be met for the scheme of arrangement to be approved.

Feedback required

Market participants were asked to provide feedback on the matters raised in the consultation paper in the form of a questionnaire which accompanied the paper. This required market participants to provide their views on:

- whether they agreed that a problem exists with the current regulatory provisions;
- whether the policy objectives outlined by the panel were appropriate for assessing how alternative solutions for effecting changes of control of Code companies should be measured;
- the five options noted above; and on
- the appropriateness of the Code's current 90% compulsory acquisition threshold. On this issue the panel is interested in determining whether such a high threshold has created an incentive for companies to utilise the reconstruction provisions instead of the Code, because 90% might be unreasonably hard to achieve.

Bell Gully's submission

The tenor of Bell Gully's submission on the Takeover Panel's consultation paper (which we provide a link to below) is our strong preference for the continued availability of the reconstruction options in their current form.

In Bell Gully's view the reconstruction provisions of Parts XIII and XV the Companies Act are important and appropriate mechanisms to achieve the objectives contemplated by the legislature when passing that Act. The existence of schemes and amalgamations means that market participants are exposed to an array of options and are able to match their individual situations with the most appropriate mechanism.

We consider that it is important for the panel to recognise that schemes have been very beneficial to companies and shareholders in New Zealand. Over the past eight years Bell Gully has been associated with a number of such beneficial schemes such as those involving Fletcher Challenge, Fisher & Paykel, Dominion Property Group, St Lukes and the INL and Sky TV merger. For its part, Bell Gully is not aware of schemes that have been approved under Part XV, yet have been prejudicial to shareholders. We were particularly concerned with the panel's reference in the consultation paper to the Waste Management transaction which used the amalgamation process under Part XIII as an example of possible prejudice. Whereas, in fact,

shareholders were well compensated for their shares in that company (and very few shareholders voted against that amalgamation).

In Bell Gully's view, the risk of adding further protections is that Parts XIII and XV lose their flexibility, making it practically impossible for certain reconstructions to be effected, or putting them at risk of being hijacked by small minorities with disproportionately large powers of veto. This issue arose during the Dominion Property Group litigation with the Takeovers Panel that went to the Court of Appeal in 2006. The panel's suggested voting regime was too stringent and may have jeopardised an arrangement that was beneficial to all investors.

In our view, the Part XV jurisdiction must be preserved and safeguarded, not rendered useless by additional safeguards that in fact are detrimental to the body of shareholders the panel is wishing to protect. By maintaining the flexibility of the current regime the competitiveness of New Zealand's capital markets internationally will be protected.

Next steps

Submissions for the paper closed on 15 February. Submissions received will be used to assist the panel to advise the Minister of Commerce on options to deal with the cross-over between the reconstruction provisions in the Companies Act and the provisions of the Takeovers Code. NZIER will also be involved in the analysis of the submissions and the preparation of a Regulatory Impact Analysis (RIA) if the panel conclude that it should recommend to the Minister that changes be made to the existing laws. The RIA will require the panel to:

- demonstrate that the status-quo is unsatisfactory;
- consider all feasible options;
- identify all environmental, economic, social (including health) and cultural costs, risks and benefits of each feasible option;
- quantify or otherwise assess each impact;
- indicate any assumptions or judgments made by policy makers; and
- indicate why the preferred option has been chosen over others.

We will keep you updated on any further developments on this matter.

To view Bell Gully's submissions on the consultation paper see www.bellgully.com or [click here](#).

For further details, visit the Takeovers Panel's website at www.takeovers.govt.nz

To view the consultation paper, visit the Takeovers Panel's [website](#) or [click here](#) to download the paper.

For further information please contact your usual Bell Gully adviser or:

[Andrew Abernethy](#)
Partner

[Andrew Brown](#)
Partner

[David Cooper](#)
Partner

Securities and capital markets

Final changes arising from Securities Legislation Bill in force on 29 February

Regular readers of Commercial Quarterly already will be aware that the last of the changes made by the 2006 Securities Legislation Bill come into effect on 29 February. In this note we provide you with a brief outline of the final key components of the Government's securities reform package which are now in place.

Background

The Securities Legislation Bill, which was passed in October 2006, represents the completion of part three of the Government's four part securities and financial market reform programme. Earlier reforms saw the introduction of the Takeovers Code in 2001 and an overhaul of regulations governing the stock exchange and listed issuers in 2002. The fourth and final part of the securities reform programme is currently underway as part of the Government's Review of Financial Products and Providers. This addresses issues relating to securities offerings under the Securities Act 1978.

The Securities Legislation Bill was passed as:

- the Securities Amendment Act 2006;
- the Securities Markets Amendment Act 2006;
- the Takeovers Amendment Act 2006; and
- the Fair Trading Amendment Act 2006.

Most of the Securities Act amendments and Takeovers Act amendments came into effect after their assent on 24 October 2006. However, several key components of the new securities law were kept on hold pending the approval of regulations. These were the Securities Markets (Substantial Security Holders) Regulations 2007, the Securities Markets (Market Manipulation) Regulations 2007 and the Securities Markets (Investment Advisers and Brokers) Regulations 2007 which were enacted by Order in Council on 3 December 2007. The regulations and the remaining provisions of the Amendment Acts noted above all come into effect on 29 February 2008.

For a complete overview of all the changes made by the Securities Legislation Bill see Bell Gully's earlier article "[Securities Legislation Bill completes parliamentary process](#)" in the Spring 2006 issue of Commercial Quarterly.

Latest changes in force

The latest key components to take effect include:

- ***new disclosure requirements for investment advisers and brokers***

A new part 4 of the Securities Markets Act 1998 together with the Securities Markets (Investment Advisers and Brokers) Regulations 2007 provide for additional disclosure obligations on investment advisers and investment brokers prior to giving advice or receiving investment money or property.

- ***a new insider trading regime***

The new insider trading provisions in the Securities Markets Amendment Act 2006 reflect a new rationale for the prohibition of insider trading. In particular, under the new law anyone can be an insider and inside information can come from any source. Formerly, a person was only an "insider" if they received the information directly or indirectly through their relationship with the public issuer.

A comprehensive overview of the new insider trading provisions is available on our website in a paper titled "[The New Insider Trading Laws](#)" presented by Bell Gully senior associate Jenny Cooper to the

Securities Legislation and Capital Markets Update conference held in Auckland in September 2007.
Also see:

- o the article [Urgent law change needed to remedy serious flaw in new insider trading laws](#) by Bell Gully partner and firm chairman Roger Partridge and senior associate Jenny Cooper; and
- o the article [Insider trading: how effective is a Chinese wall defence?](#) in the Winter 2007 Commercial Quarterly for some insight into how the New Zealand courts may assess the effectiveness of a Chinese Wall defence to an allegation of insider trading.

- ***new law on market manipulation***

Dedicated provisions in the Securities Markets Act 1988 prohibiting forms of market manipulation (or market rigging) have been introduced under the new regime. Three new offences are created for manipulating or interfering with the operation of a securities market. The rules are intended to prohibit practices that are considered to impermissibly affect the price of listed securities and distort the operation of the market in listed securities.

- ***changes to the substantial security holders' disclosure regime***

The basic features of the substantial security holders' disclosure regime contained in the Securities Markets Act 1988 have not changed under the new law, but the law has been amended to clarify and simplify the situations in which disclosure is required with a view to reduce compliance costs over the medium to long term.

The new Securities Markets (Substantial Security Holders) Regulations 2007 require some changes to the information that needs to be disclosed when releasing a Substantial Security Holder notice to the market. Under the new regulations there are three types of disclosures of Substantial Security Holdings:

- disclosure of beginning to have substantial holding;
- disclosure of movement of 1% or more in substantial holding or change in nature of relevant interest or both; and
- disclosure of ceasing to have substantial holding.

The Regulations allow NZX to set or change the forms and delivery methods for each of the above event disclosures with the Minister of Commerce's approval. At this stage it appears that NZX has chosen to use the same forms set out in Schedule 1 of the Regulations. As required by the Regulations, NZX has made the approved forms available on its website.

To access these forms from the NZX's website [click here](#). Note also that under Regulation 4(2)(a) NZX requires these forms to be completed in either word or plain text format and emailed to announce@nzx.com.

In addition to the above disclosure notices, the Regulations also specify forms for a public issuer to use when it requires a person to disclose relevant interests to it under section 35 of the Securities Markets Act or disclose information to it under section 35A of the Act.

- ***extended liability for the continuous disclosure regime***

The new part 5 of the Securities Markets Act 1988 contains amended remedies for a contravention of the continuous disclosure obligations. The expanded definition of contravene which is provided by part 5 has the ability to capture senior management who are involved in a contravention by a public issuer of the continuous disclosure obligations. For further details on this topic please refer to our article "Expanded liability under the continuous disclosure regime" which was published in the [Winter 2007 Commercial Quarterly](#)

- ***changes to the takeovers regime: truth in takeovers***

The remaining provisions of the Takeovers Amendment Act 2006, which come into force on February 29, introduce market manipulation prohibitions to apply in relation to takeovers. The provisions are broad and cover communications outside the formal offer, target company statement and independent advisers document; with the changes likely to have a significant impact on the way takeovers are run given that many takeovers are won through these communications. For further

details on these changes please refer to the article ["Truth in takeovers: market participants should prepare for a more rigorous approach"](#) in this issue of Commercial Quarterly.

New Securities Law website and Guide

In 2007 the Securities Commission set up a website (www.newsecuritieslaw.govt.nz) to help people understand the new securities law. The general scope of the new law is explained on the website and people can register to receive updates as they become available. The website includes a collection of articles and news releases on the new law.

The Securities Commission has also prepared a ["Guide to the New Securities Law 2008"](#) which explains the changes made to the Securities Act 1978 and the Securities Markets Act 1988.

An overview of the new securities law was also published in the Securities Commission's publication, [The Bulletin](#), No 38, January 2007 with a follow up article in [The Bulletin](#) No.42, January 2008 which focuses on the commission's powers to enforce the new rules, penalties and compensation.

Competition and consumer law

Commission to review internal merger clearance process

The Commerce Commission has signalled that it intends to review the processes it follows when dealing with merger clearance applications. In this article Bell Gully senior associate David Blacktop explains why Bell Gully sees this as a positive move with the potential to provide greater certainty, and demystify the clearance process, for businesses. However, commission resource constraints and the complexity of the issues raised will continue to determine how soon a decision is reached in any particular case.

Serious cartel conduct - coming to a jail near you?

In this article senior associate Simon Ladd considers the implications for New Zealand companies and individuals operating on both sides of the Tasman if the Australian Government's recent proposal to introduce criminalisation of cartel conduct is implemented.

Competition and consumer law

Commission to review internal merger clearance process

The Commerce Commission has signalled that it intends to review the processes it follows when dealing with merger clearance applications. In this article Bell Gully senior associate David Blacktop explains why Bell Gully sees this as a positive move with the potential to provide greater certainty, and demystify the clearance process, for businesses. However, commission resource constraints and the complexity of the issues raised will continue to determine how soon a decision is reached in any particular case.

The Commerce Act provides a pre-acquisition clearance regime under which potential acquirers can apply to the Commerce Commission for approval to make an acquisition. To grant approval, the commission must be satisfied the acquisition would not substantially lessen competition. The Act requires the commission to make a decision within 10 working days of receiving an application, although there is broad agreement that this timeframe is unrealistic.

The more usual time frame is in excess of 40 working days with latest indications from the commission being that it aims for a 45 working day turnaround. Why do firms allow the commission to take so long when the Act requires a 10 day turnaround? The Act provides that if the commission is not *satisfied* there is no issue (e.g. because it does not have sufficient time to reach a considered view), it must decline the application. Facing a request for an extension, this gives the applicant a Clayton's choice.

As part of the proposed amendments to the Commerce Act the commission has suggested the statutory timeframe be extended to 40 working days. However, notwithstanding this extension, there is no guarantee that a decision will be reached in this time period – commission resource constraints and the complexity of the issues raised will continue to determine how soon a decision is reached in any particular case.

Following a review of its processes the commission has indicated it intends to introduce Process Guidelines aimed at providing more clarity for applicants. The commission intends to release these for consultation later this year, prior to finalisation. To date the advice received by the commission is that the process should include:

- Providing applicants with a draft timeline for the investigation at an early stage.

We support this because it would (a) increase transparency, and (b) provide a visible benchmark against which progress could be measured.

- Issuing a key issues statement about the middle of the investigation (days 20-25).

This could set out issues on which the commission is satisfied and issues which require further analysis. This is similar to the ACCC's statement of issues, although might not be as comprehensive. We support this move because it would assist applicants and their advisers to focus their efforts on addressing the key issues. While as a matter of practice, the key issues often becomes clear as an investigation progresses, it is often difficult to say with certainty that a particular issue is "off the table".

- Updating the applicant on timing after the key issues statement has been issued and considering further information on key issues.

- Having considered the key issues, the commission might grant approval. However, where it is minded to decline approval it will then issue a Letter of Concern and allow the applicant to make further submissions. The commission already adopts this process.

While the detailed draft process guidelines need to be considered carefully when they are published, we consider this is a very positive step which has the potential to demystify the application process for applicants. Clear communication of timeframes is, we think, critical to providing business with the necessary certainty while balancing the need for the commission to undertake the investigations necessary to perform its functions.

Competition and consumer law

Serious cartel conduct - coming to a jail near you?

In this article senior associate Simon Ladd considers the implications for New Zealand companies and individuals operating on both sides of the Tasman if the Australian Government's recent proposal to introduce criminalisation of cartel conduct is implemented.

In a paper in November last year ("Recent Developments, Trends, and Milestones in the Antitrust Division's Criminal Enforcement Program"), Scott Hammond, Deputy Assistant Attorney General of the United States Department of Justice (DOJ), stated:

"The carrot and stick enforcement strategy of coupling the Division's Corporate Leniency Program with severe sanctions and use of all available investigatory tools to create a significant fear of detection, both inside and outside the United States, has succeeded in cracking dozens of international cartels, securing convictions and jail sentences against culpable U.S. and foreign executives, and obtaining hefty corporate fines. The Division has steadfastly emphasized the importance of individual accountability and stiff corporate fines to optimize deterrence of cartel conduct."

In 2007, sentences for breaches of the United States' Sherman Act involved a record 31,391 jail days, with an average sentence of 31 months, and over US\$630 million in criminal fines. The DOJ currently has 135 pending grand jury investigations, including over 50 investigations of suspected international cartels.

With the Australian Government's publication late last year of the *Discussion Paper: Criminal Penalties for Serious Cartel Conduct* the criminalisation of cartel conduct has come a significant step closer to home.

The Discussion Paper follows on from the 2003 Dawson Review's recommendation that "serious or hard-core cartel activity may be sufficiently reprehensible to be punishable by the imposition of a gaol sentence" and reflects the Australian Government's commitment to introducing a bill into Parliament this year to criminalise such conduct under the Trade Practices Act 1974 (the TPA).

Many of the concepts underpinning the exposure draft of the Trade Practices Amendment (Cartel Conduct and Other Measures) Bill 2008, released for consultation with the Discussion Paper, are familiar from the existing civil liability provisions of the TPA and our own Commerce Act. The key ingredients of the proposed offences are:

- making a contract or arrangement or arriving at an understanding *or* giving effect to a contract, arrangement, or understanding;
- which contains a "cartel provision", i.e., a provision relating to price-fixing; restricting outputs in the production and supply chain; allocating customers, suppliers or territories; or bid-rigging;
- by parties that are, or would otherwise be, in competition with each other.

The ingredient that would distinguish criminal from civil liability is a dishonesty requirement - the intention of dishonestly obtaining a benefit. The prosecution would need to prove the relevant conduct was dishonest according to ordinary peoples' standards and known by the defendant to be dishonest according to ordinary peoples' standards. Such a requirement is the standard for criminal liability for serious cartel conduct under the United Kingdom's Enterprise Act 2002 (with which the Australian draft legislation has much in common) and already exists in other areas of Australian law, e.g., in the Commonwealth Criminal Code Act 1995 and Corporations Act 2001.

The proposed maximum penalties for individuals are imprisonment for five years and a fine of A\$220,000 (as compared to five years and an unlimited fine in the United Kingdom or ten years or US\$1 million in the United States). For corporations the maximum fine is the greater of A\$10 million or three times the value of the benefit from the cartel or, where that cannot be determined, 10% of annual turnover (as compared to US\$100 million in the United States; there is no criminal liability for corporations under the Enterprise Act).

A draft Memorandum of Understanding (MOU) released with the Discussion Paper proposes that the ACCC will investigate suspected criminal cartel offences and refer such conduct to the Commonwealth Director of Public Prosecutions (DPP) for prosecution. The ACCC would also manage the civil and criminal immunity processes, with the DPP deciding whether to grant immunity in criminal proceedings.

In deciding whether to refer a matter to the DPP, the ACCC would consider the duration and market impact of the conduct, the detriment caused to the public, and whether the value of affected commerce or bids exceeded A\$1 million within a 12 month period. In deciding whether to prosecute, the DPP would consider the cartel's impact, the scale of the detriment caused to consumers and the public, and any previous admissions to or convictions for cartel conduct. Although the MOU records that "Criminal investigations and prosecutions will be targeted at serious cartel conduct, and relatively minor conduct will ordinarily be pursued civilly", it also states that "some matters may warrant both criminal and civil proceedings".

Criminalisation of serious cartel conduct has been considered previously in New Zealand. In a January 1998 discussion document, "Penalties, remedies and court processes under the Commerce Act 1986", the Ministry of Commerce concluded that "hard core cartelisation is a far more serious offence than the civil law offence of insider trading ... and the consequences of price fixing to New Zealand society seem to be more akin to tax and customs duty evasion". Although not currently on the legislative radar, it seems inevitable given the international trend towards criminalisation of serious cartel conduct in general (countries that have criminal sanctions for cartel conduct include the United States, Canada, the United Kingdom, France, Ireland, Norway, Germany, Austria and Japan) and harmonisation of trans-Tasman business laws in particular that the issue will be considered again here. Those trends and the existing criminal liability for white collar offences such as tax and customs evasion and (from 29 February) insider trading mean that the odds of similar amendments to the Commerce Act in time must be high.

If the Australian legislation is passed later this year, there will of course be more immediate implications for New Zealand companies and individuals operating on both sides of the Tasman. To the extent those companies and individuals are involved in cartel conduct in Australia they will be directly exposed to the risk of prosecution. To the extent there is parallel conduct in New Zealand, they face an increased risk of detection here because criminalisation of serious cartel conduct increases the incentives to seek leniency and a cartel member seeking leniency in Australia will almost inevitably seek leniency in both jurisdictions. As the Commerce Commission's General Counsel, Peter Taylor, stated in a 2007 paper, "The Application of the Leniency Policy":

The commission will watch developments in Australia with interest. In the meantime, it notes the sentiment of the US DOJ that:

"Nothing in our enforcement arsenal has as great an effect as the threat of substantial incarceration in a United States prison - nothing is a greater deterrent and nothing is a greater incentive for a cartel member, once exposed, to cooperate in the investigation of his co-conspirators".

[Click here](#) to read the discussion paper, exposure draft of the legislation and MOU.

Submissions close on 29 February 2008.

This article was first published in NZLawyer, 8 February 2008.

Intellectual property and information technology

What's in a name? The importance of getting a business name right

In this article senior solicitor Jeanette Singh looks at a recent case before the courts which highlights the importance of conducting the appropriate due diligence before choosing a business name or launching a brand.

New guidelines on technology IP set to move ownership from government hands

In this article senior associate Heidi Leslie and summer clerk Luke Hayward review the State Services Commission's new guidelines for the Treatment of Intellectual Property Rights in ICT Contracts.

Privacy in the online world

Debate has been ignited over what exactly constitutes personal information amid growing concern about online privacy. In this article senior associate Heidi Leslie looks at the European debate and why it triggers a reminder for New Zealand business.

Intellectual property and information technology

What's in a name? The importance of getting a business name right

In this article senior solicitor Jeanette Singh looks at a recent case before the courts which highlights the importance of conducting the appropriate due diligence before choosing a business name or launching a brand.

Business owners need to be careful not to use a name or brand which is so close to a competitor's that confusion is likely to arise. Even if a business name is not registered as a trade mark, the party who first commenced use of the business name may prevent the other from using it by relying on provisions of the Fair Trading Act and the laws of passing off. Targeted searches will clarify whether the name is available for use and will save the heartache of a challenge after you have launched, with the possibility of losing the investment in building a name or brand and the added cost of establishing a new one.

The case

Background facts

In a recent High Court case⁴, Great Barrier Airlines Limited (the appellant) sought an injunction to prevent its competitor, Commercial Helicopters Limited trading as Great Barrier Air (and various related parties together referred to as the respondents), from trading under, using and advertising any name similar or identical to GREAT BARRIER AIRLINES or GREAT BARRIER EXPRESS on the grounds that such conduct amounted to a breach of the Fair Trading Act and the laws of passing off.

Both the appellant and the respondents have been competing in the market for flight services to and from Great Barrier Island for a considerable time. The appellant has been using and trading under the name GREAT BARRIER AIRLINES since as early as 1995. The respondents have provided flights under the names GREAT BARRIER XPRESS (following an arrangement with the appellant in 1998 when it had its transport operator's licence suspended for a brief period) and MOUNTAIN AIR.

It would appear that the respondents incorporated the company GREAT BARRIER AIR LIMITED in mid-2006 as a counter-measure to the appellant being re-allocated the Yellow Pages listing for the name Great Barrier Xpress. This meant in practice that the name GREAT BARRIER AIR LIMITED was listed in the New Zealand White and Yellow Pages immediately above the appellant's listing for GREAT BARRIER AIRLINES. At the same time the respondents abandoned their listing for their former principal trading name of Mountain Air.

The District Court declined to grant an injunction finding that the respondent's actions did not amount to a misrepresentation and that the plaintiff did not demonstrate that it would actually suffer loss.

Appeal to the High Court

The appellant appealed the District Court decision on the grounds that the judge had failed to take into account the claim advanced under the Fair Trading Act (misleading and deceptive conduct) and had applied a wrong principle in requiring the plaintiff prove on the balance of probabilities that it would actually suffer loss.

Judgment

Justice Winkelmann found that the District Court judge had erred in that he did not turn his mind to the cause of action under the Fair Trading Act and had only considered the passing off action. She also found that the judge had applied the wrong test in requiring the appellant prove that it had suffered actual loss on the balance of probabilities. She stated that it is essential to a passing off action that the defendant's

⁴ *Great Barrier Airlines Flight Operations Limited v. Great Barrier Air Limited (first respondent), Commercial Helicopters Limited (second respondent) and Keith Leslie and Robyn Malcolm McKenzie (third respondent) (Unreported Decision, High Court, Auckland Registry, Winkelmann J., 13 December 2007, CIV 2007-404-5710)*

activities cause substantial damage to the plaintiff's business or goodwill or are likely to do so if continued. Where the services of both parties compete (as in the present instance), then it is likely that the plaintiff will suffer loss. At an interlocutory stage, it is not necessary for the appellant to prove loss; all it needed to prove was that it was likely to suffer damage as a result of confusion caused by the respondents' conduct.

Section 9 of the Fair Trading Act provides that "no person shall, in trade, engage in conduct that is misleading or deceptive or is likely to mislead or deceive".

To be successful under this cause of action, the appellant had to prove that the first respondent's listing in the telephone directories is misleading and deceptive conduct. Because the appellant and respondents both operated in the same market (air travel to the Great Barrier Island), Justice Winkelmann accepted that consumers may be misled or deceived by the lack of distinctiveness of the telephone directory listings. She stated as follows:

"I am satisfied that the appellant has a strong case that the respondent's conduct breaches section 9. The names GREAT BARRIER AIR LIMITED and GREAT BARRIER AIRLINES are so close that confusion is inevitable. Imperfect recollection of the relevant sectors of the public must be taken into account. A person searching the directory for the GREAT BARRIER AIRLINES number will be most unlikely to differentiate that company from GREAT BARRIER AIR."

Counsel for the respondent argued that that there was no serious question to be tried because the injunction was sought against Great Barrier Air Limited (the first respondent) who was not in trade. However, Justice Winkelmann stated that in reality all respondents were closely related and worked collaboratively to ensure that the name GREAT BARRIER AIR was available for the second respondent (Commercial Helicopters Limited) to use. Therefore, this was use in trade. The respondents opposed the injunction by arguing that damages would be an adequate remedy. However, Justice Winkelmann disagreed stating:

"If injunctive relief is not granted, the appellant's goodwill in its trading name will be potentially eroded by the confusion..."

In granting the injunction her honour ordered the respondents to stop use of the name GREAT BARRIER AIR in any form until the issues were resolved at trial.

How to get it right

Before launching a new business name or a brand, it is important to conduct searches of the various official registers (including the Intellectual Property Office of New Zealand (IPONZ) trade marks register and companies office register) to ensure that no other trader is using or holds a trade mark registration for a similar or identical name/trade mark. Conducting due diligence in the beginning can save you from heartache and expensive litigation in the future if another trader objects to your use of the name.

Intellectual property and information technology

New guidelines on technology IP set to move ownership from government hands

In this article senior associate Heidi Leslie and summer clerk Luke Hayward review the State Services Commission's new guidelines for the Treatment of Intellectual Property Rights in ICT Contracts.

New guidelines just released on who owns the intellectual property rights around government technology projects break new ground.

They reverse the previous unofficial default position over ownership of IP, bringing New Zealand into line with other countries such as Australia – and have the overarching aim of freeing up government-generated technology for commercialisation.

The State Services Commission has released the Guidelines for Treatment of Intellectual Property Rights in ICT Contracts to assist government and public sector agencies better align their positions on intellectual property and to understand the key drivers behind ownership and licensing positions.

Up until now the unofficial position has been the government body that commissioned the work should be the owner of the IP, on the theory that ownership would give the government greater control, flexibility, potential future cost-savings and future proofing.

The new guidelines endeavour to reverse this stance so that the supplier should own the new IP and grant licences to its public sector customers.

The rationale behind this approach is that exploiting newly created IP is not generally part of the core business of state sector entities. By holding onto the ownership of IP they may stifle commercialisation opportunities that could benefit New Zealand's economic development.

As the guidelines point out, the "government is often a major player in the creation of new intellectual property, but rarely seeks to commercialise it". The change in IP ownership would help create opportunities for the business sector which has the commercial profit motive critical to successful commercialisation.

Essentially the new guidelines recommend three options for the treatment of IP in ICT contracts:

1. the government body owns the IP;
2. the government body owns the IP but grants a licence back to the supplier; or
3. the supplier owns the IP and grants a licence to the government body commissioning the work and all other government agencies.

The third option is described as the default. In reality, however, it only appears to be the default where the IP is not part of a critical government ICT system and the contracted deliverables mainly use the supplier's pre-existing IP or there is no need for the government to retain ownership.

There is no guidance (and therefore flexibility) on how to determine whether the contracted deliverables mainly use pre-existing IP (this could be measured, for example, by percentage in terms of content, criticality to the system or price). There is no mention in this formula of pre-existing third party IP (i.e. IP that belongs to neither the supplier nor the government), so we have to assume that, under the guidelines, the "supplier's pre-existing IP" includes IP provided by third party.

The guidelines recommend that the government body should own the IP only if any of the following circumstances apply:

- there are security or integrity reasons for the government body to own the IP;
- the IP applies to a critical government system;
- the government wants the ability to enforce the IP against infringers;

- other public sector agencies are the only likely users of the IP;
- the government body wants a third party other than the original supplier to be able to commercialise the IP;
- the government body intends to allow free use of the IP on open source terms;
- there are other reasons why the government body does not want the original supplier to own the IP.

Government suppliers will need to be aware that these guidelines are not law and that giving effect to the third option of supplier ownership will require express contractual provisions to that effect. For example, under the Copyright Act, the Crown owns all copyright in works commissioned under contracts for services unless the contract specifically provides otherwise. IP ownership clauses between the supplier and the government will need to be carefully and thoughtfully drafted to give effect to option three of the guidelines. The guidelines helpfully provide sample clauses to be used for this purpose.

Overall, the new guidelines give the government more flexibility in negotiating its IP position in ICT contracts. They also offer good insight into the relative benefits and disadvantages of government ownership of IP and some transparency to the rationale behind positions on IP ownership. The decision to implement new guidelines is a positive move which has the potential to add value to the New Zealand economy and the ICT community.

For a copy of the guidelines visit: www.e.govt.nz/policy/ipr

Intellectual property and information technology

Privacy in the online world

Debate has been ignited over what exactly constitutes personal information amid growing concern about online privacy. In this article senior associate Heidi Leslie looks at the European debate and why it triggers a reminder for New Zealand business.

Privacy in the online world is taking another interesting twist in Europe, fuelled by a call for internet protocol (IP) addresses to become protected information.

But in New Zealand our privacy laws may already afford the protection should a potential breach be questioned.

Each computer is assigned an IP address – a series of specific numbers that can be used to identify it and its user. During hearings into online data protection in the European Parliament last week, came a call from the head of the European Union's privacy regulators for IP addresses to be protected as if they were sensitive personal information.

This statement has caused a stir, particularly among search engines such as Yahoo and Google, who typically collect IP addresses to help refine search results – and localise or personalise its online advertisements.

While clearly not everyone believes that IP addresses are personal information, it is a view that is consistent with the spirit of privacy laws around the world: information that can be used to identify individuals should be protected.

Under the New Zealand Privacy Act, "personal information" means information about an identifiable individual. Given that an IP address is unique code assigned to a particular computer and identifiable individuals can then be linked to their computer, it is prudent to treat those IP addresses as personal information for the purposes of the Privacy Act.

Companies and individuals that collect IP addresses should be aware that the obligations of the Privacy Act may apply to IP addresses, just as they do to individuals' names, addresses, phone numbers and other personal details. They ought to comply with the requirements of the Privacy Act when it comes to collecting, storing, protecting and sharing IP addresses or may find themselves on shaking ground in the event of a breach.

In the meantime in Europe the debate continues, with the search engines and other internet organisations touting the possibility of a self-regulation framework rather than face new laws with potential to have a major impact on online advertising and the search engine business.

This article was first published in the Dominion Post, 28 January 2008.

Utilities and resources

A round up of the latest developments in the electricity sector

The electricity sector continues to move forward with a number of new laws in the pipeline. This update includes commentary on the Electricity Industry Reform Amendment Bill; the proposed legislative provisions which will give effect to the government's preference for new renewable electricity generation and the latest changes proposed for the Electricity Governance Rules.

Efficiency thresholds remain important for lines businesses

The Commerce Commission recently published a discussion paper on re-setting the efficiency thresholds of its targeted control regime for large electricity lines businesses for the 2009 to 2014 period. In this article senior associate David Blacktop outlines why the commission's current price/quality path thresholds reset remains important for electricity lines business (and potentially for other sectors as well), despite the announced changes to the price control regime for electricity lines business.

Key issues for the forestry sector from the Climate Change (Emissions Trading and Renewable Preference) Bill

New mechanisms to combat climate change mean the cost of carbon has now become a commercial reality for New Zealand business with the forestry sector at the forefront of the Government's policy initiatives in this area. In this article senior associate Kate Radka outlines the essential features of the emissions trading scheme for the forestry sector proposed under the Climate Change (Emissions Trading and Renewable Preference) Bill and sets out some questions to help foresters develop a strategy for managing their financial exposure to carbon.

Utilities and resources

A round up of the latest developments in the electricity sector

The electricity sector continues to move forward with a number of new laws in the pipeline. This update includes commentary on the Electricity Industry Reform Amendment Bill; the proposed legislative provisions which will give effect to the government's preference for new renewable electricity generation and the latest changes proposed for the Electricity Governance Rules.

Electricity Industry Reform Amendment Bill

The purpose of this Bill is to implement three main policy changes aimed at making it easier for lines companies to invest in generation by removing unnecessary barriers to investment without creating opportunities for the rise of unwarranted market power.

The Electricity Industry Reform Act 1998 (EIRA) required full ownership separation between electricity lines and electricity supply businesses. Two subsequent amendments, in 2001 and 2004, relaxed the rules on ownership separation to an extent: in 2001 the Act was amended to enable lines companies to invest in new renewable generation without limit (provided it was made in accordance with corporate separation and arms-length provisions in that Act), and to own any generation up to the higher of 5MW or 2% of lines peak load; the 2004 amendment allowed lines companies to own generation up to 50MW or 20% of peak load and unlimited reserve generation contracted to the Electricity Commission, to improve security of supply.

The Electricity Industry Reform Amendment Bill (the Bill) further relaxes the ownership separation rules and restrictions. This is done in three ways:

- By making it easier for owners of lines businesses to sell the output of the generation they were permitted to own under the 2001 and 2004 amendments to the EIRA. A number of amendments are proposed to achieve this objective. Under the proposed amendments, owners of lines businesses will be allowed to sell up to 100% of the nominal annual output capacity of permitted generation, and to trade such permitted generation via financial hedges. The proposed amendments are also aimed at lowering the cost of corporate separation and compliance with arm's length rules by raising the threshold for requiring compliance from 5MW or 2% of maximum demand to 10MW, allowing the same person to be a director of both lines and supply businesses, while requiring at least one independent director and not permitting executive directors, and allowing the same person to be a manager of both companies up to a threshold of 30MW. The lines company is also permitted to utilise the same staff and premises for its lines business and its supply business. This makes it more attractive for owners of lines businesses to invest in permitted generation.
- By narrowing the scope of ownership separation requirements to focus on the geographic areas of operation of the lines business and the supply business. This is achieved by allowing owners of lines businesses to be involved in generation and retailing without limits outside their lines area. The Bill also proposes removing the requirements for corporate separation and compliance with the arm's length rules for supply businesses undertaken by a lines company outside of its lines area. The rationale behind these amendments are that the lines company is likely to have the potential to exercise market power and to engage in anti-competitive practices if it is supplying electricity within its lines area, but there is likely to be no such potential when the lines business and supply business are geographically separate. These changes are consistent with the decisions of the Commerce Commission in the applications for exemption by Eastland Networks Limited (Decision No 575) and Unison Networks Limited (Decision No 576). In those decisions the Commerce Commission placed considerable emphasis on the geographic separation of the lines and supply businesses.
- By amending the definition of "renewables" to include all renewables. Previously the definition included only new renewable technologies, and excluded hydro and geothermal generation using traditional technologies. The new definition includes all renewables to reflect the Government's policy of encouraging the development of renewable energy.

The Bill was introduced on 4 December 2007, with submissions due by 29 February 2008. The Select Committee is due to report on the Bill by 10 June 2008. We will continue to monitor developments in this

area, and will look to provide an update in this publication once the Select Committee report has been released.

Climate Change (Emissions Trading and Renewable Preference) Bill

A guiding principle in the New Zealand Energy Strategy (NZES) is that in future it is preferable that all new electricity generation be renewable, except to the extent required to maintain security of supply. This has been reflected in the proposed amendments to the Electricity Act 1992 set out in the Climate Change (Emissions Trading and Renewable Preference) Bill, which introduces a 10-year moratorium on almost all new fossil fuel generation.

The moratorium applies to new base-load thermal electricity generation above 10 megawatts that uses more than 20% oil, coal or gas as its fuel source, although there will be scope for exemptions to be made by the Minister of Energy on the recommendation of the Electricity Commission for specific fossil-fuelled generation proposals that address concerns over security of supply.

Whilst the proposed amendments to the Electricity Act certainly reflect the principle set out in the NZES, the question arises as to whether the moratorium is necessarily required. On its own the impending emissions trading scheme provides clear price signals against thermal generation. The introduction of the proposed moratorium alongside the emissions trading scheme, which effectively forces generators to invest in renewable energy regardless of whether this is the lowest or highest cost option, could be seen as acting counter to the purpose of the Bill, namely "reducing New Zealand's net emissions... and complying with our international obligations, including our Kyoto Protocol obligations, while maintaining economic flexibility, equity, and environmental integrity".

RMA call-in for renewable energy projects

The Government signalled in its New Zealand Energy Strategy to 2050 (NZES) released in October 2007, that in the future it expects more projects will be called-in under the existing provisions of the Resource Management Act (RMA). Under section 141A of the RMA, the Environment Minister can call-in a proposal and direct that the matter is referred to either a Board of Inquiry or the Environment Court. This means that the matter is decided by either of these two bodies instead of the relevant district, city or regional councils.

In late January 2008 Environment Minister Trevor Mallard called-in two renewable energy development proposals under the RMA, namely:

- the Unison Te Waka proposal for a 34 turbine wind farm at Te Waka near the Napier-Taupo Road (which has been referred to the Environment Court); and
- a new geothermal power station called Te Mihi being developed by Contact Energy (which has been referred to a Board of Inquiry).

The Minister has stated that the proposals were called-in because of their national significance in respect of their relevance to New Zealand's international obligations to the global environment, in terms of the Kyoto Protocol. That is, if they are approved the proposed projects will contribute to the NZES target of having 90% of our electricity generation as renewable energy by 2050.

Submissions on both proposals were called for on 8 February and close on 7 March 2008.

For more details on both of these proposals visit the Ministry for the Environment's website www.mfe.govt.nz or [click here](#) for details on the Unison proposal and [click here](#) for details on Contact Energy's proposal.

Update on Transpower's North Island Grid Upgrade Proposal

Another proposal to be called-in under section 141A of the RMA is Transpower's North Island Grid Upgrade Proposal. Decisions for that proposal have been referred to a Board of Inquiry which means that the Board of Inquiry will make decisions regarding the Notices of Requirement, instead of the nine affected councils. The call-in process effectively combines the councils' consideration and the Environment Court appeal process.

The Minister stated that he called in Transpower's proposal because he considers the proposal to be a project of national significance on the basis that the proposal:

- has aroused widespread public concern and interest regarding its actual or likely effect on the environment;
- involves significant use of natural and physical resources;
- affects more than one region or district;
- involves technology, processes or methods which are new to New Zealand and which may effect the environment; and
- is likely to result in or contribute to significant or irreversible changes to the environment.

A section 42A Report, commissioned by the Board of Inquiry under section 42A of the RMA, has been prepared for the North Island Grid Upgrade Proposal. It includes key issues of the proposal, an overview of the notices of requirement documentation and resource consent applications lodged, and an analysis of information provided by Transpower. The Board of Inquiry has also made public the submissions received by the Minister and a pre-hearing timetable on Transpower's proposal. The proposal hearing is expected to start on the 25 March 2008.

For further information on the Board of Inquiry hearing visit the Ministry for the Environment's website (www.mfe.govt.nz) or [click here](#).

Electricity Governance Rules: Obligatory testing of physical assets

The Electricity Commission is continuing with its proposed changes to the Electricity Governance Rules to require asset owners to carry out mandatory testing of their plants in order to ensure an acceptable level of asset owner compliance with obligations in Part C of the Rules. Having considered submissions on its draft rule amendments in its April 2007 consultation paper, in December the commission issued further changes to its rule amendment proposal to:

- clarify the meaning of the proposed amendments; and
- improve the consistency of asset testing obligations across different categories of assets.

Submissions on the updated proposed rule amendments closed on 8 February. To access a copy of the commission's second round consultation paper visit the Electricity Commission's website (www.electricitycommission.govt.nz) or [click here](#).

If you have any questions on any of the items noted in this update please contact:

[Garry Downs](#)

Partner

[Clive Taylor](#)

Partner,

from our Auckland corporate department, or

[Andrew Brown](#)

Partner

[Chris Gordon](#)

Partner,

from our Wellington corporate department.

Utilities and resources

Efficiency thresholds remain important for lines businesses

The Commerce Commission recently published a discussion paper on re-setting the efficiency thresholds of its targeted control regime for large electricity lines businesses for the 2009 to 2014 period. In this article senior associate David Blacktop outlines why the commission's current price/quality path thresholds reset remains important for electricity lines business (and potentially for other sectors as well), despite the announced changes to the price control regime for the electricity lines business.

Current regime

The Commerce Commission is responsible for determining whether to control the services provided by New Zealand's 29 electricity lines businesses under Part 4A of the Commerce Act. The commission has set price and quality thresholds to identify those businesses that are candidates for control. The commission uses a CPI-X price path threshold which is set for a five year period. This allows a lines company to increase its prices by an amount equal to CPI-X each year, with each firm being allocated an X value. The Supreme Court has recently affirmed this approach.

The current five year regulatory term expires on 31 March 2009. The commission has commenced consultation on price and quality path thresholds that will apply for the 2009 to 2014 period. In setting out its consultation process, the commission commented that "While no preliminary decision has been made on the form of thresholds, the commission is of the view that the current broad structure should form the initial basis for the new regime".

Proposed legislative changes

This reset process takes place with the Government's announced amendments to the price control regime for the electricity lines business ready to be introduced to Parliament. Minister of Commerce Hon Lianne Dalziel has indicated as recently as last week that she intends to introduce the Commerce (Regulated Goods and Services) Bill into the House mid-March 2008, and in her view there is potential for this bill to be passed prior to the election.

These changes repeal the existing regime and replace it with a new regime under which the Commerce Commission will have a broader range of control options. A key change is that lines businesses would be subject to a default/customised price path regime. Under this new regime the commission would set:

- o a default price-quality path (like the current thresholds); but
- o provide an ex-ante, time-bound opportunity for a firm to seek a customised path (e.g., where it needs to make a step-change in investment to maintain quality standards required by consumers).

This change has been introduced because lines companies have been concerned about the lack of investment certainty the current regime provides. Investment requires a return, however gaining that return can cause companies to breach their price path thresholds. Under the current regime, this requires lines companies to effectively make decisions and then justify those investment decisions to the commission.

The customised regime will provide an opportunity for firms to seek pre-approval and certainty for investments.

Default path still important

The practical reality is that the default path will continue to apply to most businesses and businesses will compete to get their customised case considered by the commission. The Government's intention is that the initial default path will be the price path thresholds, meaning that the current review retains a vitally important role for lines companies.

More broadly, as it will become the first default path under the new regime, it is likely to also be relevant for other sectors that may be subject to a default regime in the future. The commission is likely to call on

its intellectual capital and learning from the electricity regime in determining a customised path for any other sector.

Process for reset

The commission published a discussion paper (*Discussion Paper on the Threshold Reset 2009*) and is currently considering submissions on this paper. It intends to issue and consult on a Methodology Paper in May/June 2008. It is intended that this will be followed by a Draft Decision Paper in late September 2008 and a Final Decision Paper in December 2008.

For more information on the Commerce Commission's review of the efficiency thresholds and to access the discussion paper visit the Commission's website at www.comcom.govt.nz or [click here](#)

Utilities and resources

Key issues for the forestry sector from the Climate Change (Emissions Trading and Renewable Preference) Bill

New mechanisms to combat climate change mean the cost of carbon has now become a commercial reality for New Zealand business with the forestry sector at the forefront of the Government's policy initiatives in this area. In this article senior associate Kate Radka outlines the essential features of the emissions trading scheme for the forestry sector proposed under the Climate Change (Emissions Trading and Renewable Preference) Bill and sets out some questions to help foresters develop a strategy for managing their financial exposure to carbon.

The Climate Change Bill introduced on 4 December 2007 is significant for the forestry sector in New Zealand. The Bill largely reflects the Government's policy announcements in September regarding the introduction of an emissions trading scheme, which over time will be economy-wide. For earlier Bell Gully commentary on this refer to the article "[New Zealand's Emissions Trading Scheme - how will it work and what are the implications for business?](#)" in the Spring 2007 Commercial Quarterly.

The essential features of the scheme for the forestry sector are:

Pre-1990 forests	Post-1989 forests
These forests will be subject to the scheme, with some exemptions mainly affecting forests under 50 hectares. Foresters will be obliged to surrender emission units for any deforestation over two hectares in accordance with the proposed methodology in the draft Climate Change (Forestry Sector) Regulations 2008, which were released for consultation this month. The Government will allocate units free to forestry scheme participants but only sufficient units to allow deforestation to continue, without additional cost, at historical deforestation rates of 5% per annum of the forest estate. Kyoto-compliant units will have to be bought on the domestic or international market to cover any deforestation not covered by the units allocated free.	Post-1989 forests are not automatically subject to the emissions trading scheme, and foresters have until 1 January 2010 to decide whether to opt in. They then earn units for the carbon sequestered but must account for any emissions from harvesting or deforestation, although their liability would not exceed the total units they have earned under the scheme.

The new legislation is not expected to be passed until mid-2008 but will then apply (along with regulations) retrospectively to the forestry sector, with effect from 1 January 2008. The first emissions reporting period for forestry scheme participants is after two years, for the period ending 31 December 2009. While the details of the Bill and Regulations are important to foresters, key issues that businesses operating in the forestry sector will need to address in the coming months include:

- **Allocation of units to pre-1990 forests.** In its September policy announcement the Government stated that units would be allocated to pre-1990 forests on a pro rata basis according to the forest size. This has not been carried through to the Bill and instead the policy is to be developed further and, once decided, will be reflected in an allocation plan. Pre-1990 foresters should be protecting their interests by advocating an appropriate allocation policy and plan to Government.
- **Rights of landowners and forestry right/lease holders.** Liability is on the landowner in respect of pre-1990 forests unless they have divested any decision on deforestation to a third party. For post-1989 forests the participant can be either the landowner or the forestry right (or lease) holder, as applicable, but either requires the agreement of the other before it can register as the scheme participant. Therefore these parties need to be communicating with each other about their intentions.

Crown Forest Licence holders are unlikely to be allocated any units under the scheme as the units attributable to Crown land are expected to be set aside for the settlement of Maori claims under the Treaty of Waitangi.

- **Trading forestry emission units.** Foresters will be the first to have emission units available for sale under the scheme. This could provide important liquidity to a market where there are expected to be more buyers than sellers. However foresters will have to consider their future land use plans carefully before selling units, as they may face having to buy back units at uncertain future prices if their plans change over time. Post-1989 foresters face similar uncertainty when deciding whether or not to opt in to the scheme. For pre-1990 foresters anticipating substantial future deforestation, with the local market likely to be short, they may well need to look to overseas markets for Kyoto-compliant units. The pricing and availability of the different types of international units can vary greatly over time, so it is not too early to start looking at purchasing options.

Initial questions for pre-1990 and post-1989 foresters to start thinking about

As the consultation period for submissions on the Bill and draft Regulations draws to an end, foresters should, at least, be considering the following initial questions as they develop their strategy for managing their financial exposure to carbon.

Pre-1990 forests

- Will the proposed NZU allocation scheme for pre-1990 forests (pro rating based on forest size) favour you as compared to the alternative options floated by the Government? If so, have you indicated your support, and if not, have you made submissions in favour of a different option?
- If there are multiple interests in relation to your forest (e.g. a landowner and forestry right/lease holder), there may be more than one person with the power to deforest and trigger liability under the emissions trading scheme. If so, have you determined who is the participant for the purposes of the emissions trading scheme?
- Do you have an interest in an unincorporated joint venture, trust, partnership, or jointly own land with others, which may result in you being jointly and severally liable under the scheme?
- Are you entitled to an exemption from the emissions trading scheme and, if so, how do you get that exemption?
- Are you involved in other projects or activities that involve pre-1990 forests, which may take you over the threshold for seeking an exemption from the emissions trading scheme?
- How do you intend to use or develop your land in future? Have you refined your strategy for use and development of the land to minimise your liabilities and maximise opportunities under the emissions trading scheme? If you are considering deforesting and changing to a new land use, have you calculated your potential liability under the proposed regulations?
- Do you have an interest in Crown forest land? Will you have an interest in Crown forest land under a future Treaty of Waitangi settlement? If so, have you determined which of the proposed options will be best for you on the basis of your proposed development or use of the land?
- Have you identified all of the carbon trading opportunities that may be available to you?
- If you are selling or buying forestry land, how will you minimise your exposure to liability, and maximise your opportunities?

Post-1989 forests

- How do you intend to use or develop your land in future? Would your proposed use and development of the land maximise opportunities and minimise liabilities that may arise under the emissions trading scheme if you opt in?
- When comparing the benefits and liabilities under the scheme, bearing in mind your proposed use and development of the land, against those under the Permanent Forest Sinks Initiative and the status quo, which is the best option for you?

- Are you a forestry right holder or lease holder of post-1989 forestry land and have you sought the permission of the landowner to opt into the emissions trading scheme, if you are intending to opt in? Is your interest in the land sufficient to enable you to do so?
- Are you a landowner with a forestry right holder or lease holder of post-1989 forest on your land? If so, have you determined who is the participant for the purposes of the emissions trading scheme?
- Do you have an interest in an unincorporated joint venture, trust, partnership, or jointly owned land with others which may result in you being jointly and severally liable if the activity in which you have an interest gives rise to obligations under the scheme?
- Have you identified all of the carbon trading opportunities that may be available to you?
- If you are selling or buying forestry land, how will you minimise your exposure to liability, and maximise your opportunities?

Climate Change Practice

Bell Gully is advising the Government on legal issues involved in the design and implementation of the NZ ETS. In 2000 we advised the Government on the potential legal framework for an emissions trading scheme and its drafting of the emissions trading aspects of the Climate Change Response Act. Bell Gully has also been advising business over the last decade on climate change matters, including advising on New Zealand's first transaction on the Chicago Climate Exchange, the sale of emissions units from New Zealand projects under the Kyoto Protocol, offset projects including wind farms and contracts dealing with the passing of carbon costs in the energy sector.

For more information, contact practice group leader [Simon Watt](#)

Bell Gully news

Flying in formation - not solo - could see Maori interests soar

With many infrastructure assets and businesses already in offshore ownership, Maori trusts and incorporations, Maori Trust Boards and iwi organisations will inevitably start teaming up to become more forceful players in the domestic economy.

One new partner and five new senior associates in Bell Gully promotions

Bell Gully has promoted six outstanding lawyers to senior roles in the firm. Auckland-based corporate lawyer Anna Buchly is the firm's newest partner while five lawyers have been promoted to the role of senior associate, they are: Stuart Evans, Tania Goatley, Mathew McKay, Kate Radka and Daniel Vizor.

M&A tables place Bell Gully top in New Zealand again

Bell Gully is again the leading New Zealand law firm advising on mergers and acquisitions, according to *Thomson Financial* figures for 2007.

Bell Gully appoints new chairman

Bell Gully has elected Roger Partridge as its new chairman. Roger has been a litigation partner since 1992 and has been head of the firm's Litigation Department since 2004. He has served on the firm's Board for seven years.

Make your online contracts binding

How prominent do terms and conditions need to be on a website in order for them to be binding? What level of assent is required - does a customer have to click "I agree" or "OK" to show that they understand and agree to the terms of the agreement?

Corporate expertise boosted by returning lawyers

Bell Gully's corporate practice has gained the expertise of two senior lawyers returning to New Zealand from the UK. Jamie Durham and Nichola Williams have joined the firm's corporate team in Auckland.

Off the shelf

Other useful articles and publications from Bell Gully

For further details and more news visit:

www.bellgully.com

Useful web links

New Zealand Government

- [Inland Revenue Department](http://www.ird.govt.nz) [www.ird.govt.nz]
- [Ministry of Economic Development](http://www.med.govt.nz) [www.med.govt.nz]
- [Ministry of Foreign Affairs and Trade](http://www.mfat.govt.nz) [www.mfat.govt.nz]
- [Ministry of Labour](http://www.dol.govt.nz) [www.dol.govt.nz]
- [New Zealand Government](http://www.govt.nz) [www.govt.nz]
- [NZ Government E-Commerce Information](http://www.ecommerce.govt.nz) [www.ecommerce.govt.nz]
- [NZ Treasury](http://www.treasury.govt.nz) [www.treasury.govt.nz]
- [New Zealand Trade and Enterprise](http://www.nzte.govt.nz) [www.nzte.govt.nz]
- [Office of the Clerk of the House of Representatives](http://www.clerk.parliament.govt.nz) [www.clerk.parliament.govt.nz]
- [Parliamentary Counsel Office](http://www.pco.parliament.govt.nz) [www.pco.parliament.govt.nz]
- [Statistics New Zealand](http://www.stats.govt.nz) [www.stats.govt.nz]

New Zealand regulatory agencies and organisations

- [Commerce Commission](http://www.comcom.govt.nz) [www.comcom.govt.nz]
- [The Companies Office](http://www.companies.govt.nz) [www.companies.govt.nz]
- [NZ Law Commission](http://www.lawcom.govt.nz) [www.lawcom.govt.nz]
- [Office of the Ombudsmen](http://www.ombudsmen.govt.nz) [www.ombudsmen.govt.nz]
- [Securities Commission](http://www.sec-com.govt.nz) [www.sec-com.govt.nz]
- [Takeovers Panel](http://www.takeovers.govt.nz) [www.takeovers.govt.nz]
- [NZ Stock Exchange](http://www.nzx.com) [www.nzx.com]

New Zealand commercial sites

- [CLANZ](http://www.clanz.org) [www.clanz.org]
- [Institute of Chartered Accountants](http://www.icanz.co.nz) [www.icanz.co.nz]
- [Institute of Directors in New Zealand](http://www.iod.govt.nz) [www.iod.govt.nz]
- [NZ Bankers' Association](http://www.nzba.org.nz) [www.nzba.org.nz]
- [NZ Business Roundtable](http://www.nzbr.org.nz) [www.nzbr.org.nz]
- [NZ Institute of Economic Research](http://www.nzier.org.nz) [www.nzier.org.nz]

Australian sites

- [Australian Financial Markets Association](http://www.afma.com.au) [www.afma.com.au]
- [Australian Securities and Investment Commission](http://www.asic.gov.au) [www.asic.gov.au]
- [Australian Stock Exchange](http://www.asx.com.au) [www.asx.com.au]

International sites

- [NASDAQ](http://www.nasdaq.com) [www.nasdaq.com]
- [New York Stock Exchange](http://www.nyse.com) [www.nyse.com]
- [United States Securities and Exchange Commission](http://www.sec.gov) [www.sec.gov]