

Commercial Quarterly

SUMMER 2007

Bell Gully





Welcome to the Summer 2007 issue of *Commercial Quarterly*, Bell Gully's digest of current corporate and commercial law issues.

Each quarter we will 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

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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/publications.

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 tel 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

KiwiSaver is on track for a 1 July 2007 start date

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Annual Leave: what to do when four turns to five

Matt McGoldrick, a member of Bell Gully's employment law team, takes a look at where employers will be after 1 April 2007 when changes to the Holidays Act 2003 boost the statutory minimum annual leave from three weeks to four weeks. He predicts that the change will not be a holiday for employers!

When does a joint venture become more than just a possibility between parties?

Hot on the heels of the Supreme Court's decision in *Chirnside v Fay* (reported in the Spring 2006 issue of Commercial Quarterly) a High Court case notes that for fiduciary obligations to arise in a commercial joint venture, there must be evidence of more than mutual trust and respect between the parties.

Government is considering whether to join the 1994 WTO Government Procurement Agreement

The Ministry of Economic Development is calling for business input into whether New Zealand businesses are currently encountering discriminatory access barriers in overseas government markets. Accession to the WTO Government Procurement Agreement is seen as being of particular value to New Zealand exporters in high-tech sectors.

Commercial business law

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A frenzy of activity is going on to establish KiwiSaver in time for the proposed 1 July 2007 start date. This particularly involves the IRD (which will act as a conduit for KiwiSaver contributions) and participants in the savings and investment industry (who will establish KiwiSaver schemes).

KiwiSaver will affect all employers. All new employees from 1 July 2007 will be enrolled in a KiwiSaver scheme unless they choose to "opt-out". At a minimum, employers will need to provide all new employees with a KiwiSaver information package. Employers will also need to deduct KiwiSaver contributions from the salary or wages of participating employees (at a minimum rate of 4%) and pass these contributions on to the IRD for payment into the relevant KiwiSaver scheme.

Employers may choose to become more involved. For example, they can select a KiwiSaver scheme for their employees and customise its terms. Employers may also wish to make use of the tax advantage provided by KiwiSaver, allowing them to pay up to 4% of an employee's salary to a KiwiSaver scheme tax free.

Employers have a number of choices to make in relation to KiwiSaver and information about it is beginning to flow from Government and savings industry participants.

We recommend that employers give early consideration to their KiwiSaver strategy.

For further information or assistance with developing a KiwiSaver strategy for your business, please contact Bell Gully Partner [Mark Todd](#).

Commercial business law

Annual leave: what to do when four turns to five

Matt McGoldrick, a member of Bell Gully's employment law team, takes a look at where employers will be after 1 April 2007 when changes to the Holidays Act 2003 boost the statutory minimum annual leave from three weeks to four weeks. He predicts that the change will not be a holiday for employers!

When the inevitable improvement in the weather happens at this time of the year, it is tempting to take annual leave now rather than at Christmas time (which would have been a sensible idea this year given New Zealand had some of the most inclement weather on record). For some whose annual leave entitlements are generous or for those who "store up" annual leave, this option is achievable. However, from 1 April this year, many more employees will have this option when the Holidays Act 2003 changes to boost the statutory minimum annual leave from three weeks to four weeks.

The move from three to four

In what has been one of the most highly publicised changes to employment law in recent times, all employees will, from the anniversary date of their employment upon or after 1 April 2007, become entitled to four weeks' leave. Employees are not entitled to the extra period until their anniversary date, rather than simply becoming entitled on 1 April.

For employees whose holiday pay is regularly paid with their salary or wages (such as employees on fixed term agreements), where their employment ends within 12 months or part way through a year, their annual holiday pay will increase from 6% to 8% of their gross earnings. This rise will only apply to any entitlements accruing after their anniversary date, so that entitlements accruing before this date remain at 6% of the employee's gross earnings.

To take account of this change, employers should review employment agreements in place and, more importantly, review their payroll systems to accommodate this legislative change. In particular, this will require a consideration of exactly what each employee's entitlement will become.

This will not be particularly difficult when it comes to the majority of employees. For example, for those working 8.30am to 5.30pm, Monday to Friday, their entitlement will rise from a minimum of 15 working days to 20 working days' annual leave.

For employees who do shift work, or for other employees who work irregular hours, this calculation will not be so easy. For these employees, an employer must analyse exactly what constitutes a "genuine working week" for that particular person (for the purposes of determining the actual amount of days that an employee will be entitled to annual leave).

The Act provides that an employer and employee may agree on how this entitlement is to be observed, provided that it genuinely constitutes a working week for that employee. The factors that should be taken into account when determining employee's entitlements include the employment agreement, work patterns, rosters and any other factors about when an employee works.

This may mean that employers who require their employees to work irregular shift patterns or other similar irregular hours may be obliged - to meet the requirement of four weeks' annual leave - to allow these employees greater than 20 working days' annual leave each year.

So how about five weeks' annual leave?

There has been a suggestion that employees who are already entitled to four weeks' annual leave should be entitled to five to maintain their position compared to those entitled simply to the statutory minimum.

For most employees, this argument is unlikely to receive any traction. Put simply, the answer will be the proper interpretation of an employee's annual leave entitlements in their employment agreement. An employee who already receives four weeks' leave (and their agreement simply states that their entitlement is to four weeks) will not be directly impacted by the amendment to the Act. In most cases, the statutory minimum has simply caught up with what were previously more generous entitlements.

A residual issue will remain over the interpretation of particular provisions of employment agreements relating to annual leave. An employee may be entitled to five weeks' leave if their employment agreement states that they will be "entitled to annual leave in accordance with the Holidays Act 2003 plus an extra week's leave" or something similar. This type of provision is more likely to be in collective agreements, and employers who are party to collective agreements should probably review the particular annual leave clauses they contain.

Chance to review employment agreements

The change to the Holidays Act should be viewed as an opportunity to perform a general review of agreements for both legislative compliance and clauses that might not otherwise be included in them. In particular, this could include:

- employee protection provisions (which provide a process for consultation obligations and transfer in the case of asset sales or restructuring);
- clauses concerning workplace policies (including email and internet policies, appropriate use of workplace resources policies and other policies which cover an employee's obligations);
- suspension provisions (as any right to suspend must be in the employment agreement); and
- medical verification clauses (which provide, among other things, for the ability for employers to require employees to submit to medical examinations in the event of absence for sickness).

So, while employees might be spending their extra week's entitlement to leave on the beach, the change will not be a holiday for employers.

For further information, please contact your usual Bell Gully adviser or one of the following members of Bell Gully's employment team:

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Commercial business law

When does a joint venture become more than just a possibility between parties?

*Hot on the heels of the Supreme Court's decision in *Chirnside v Fay* (reported in the Spring 2006 issue of [Commercial Quarterly](#)), a High Court case notes that for fiduciary obligations to arise in a commercial joint venture there must be evidence of more than mutual trust and respect between the parties.*

The background facts

The issue in this case¹ was whether the parties had entered into a binding joint venture arrangement in relation to the acquisition and development of some land (owned by the Crown) in addition to an earlier financial arrangement between the parties concerning some litigation over the same land. In the alternative, the plaintiff argued that if a binding agreement was not established on the facts then the defendant nevertheless was in breach of his fiduciary duty to the plaintiff arising from the parties dealings with each other over the land.

The parties were well known to each other and had a history of various commercial dealings prior to the matter which gave rise to these proceedings.

The initial relationship between the parties in respect of the land had arisen when the plaintiff provided finance to pay the legal costs to resolve a claim taken by a third party vendor against the Housing Corporation for the release and offer of the land to that vendor. The resolution of this claim was a necessary preliminary step to the defendant being able to acquire the land. The funding of this claim was the subject of a separate deed under which the parties were to receive a 50/50 split of any immediate cash settlement made by Housing Corporation to settle the claim.

Following the successful resolution of the claim against the Housing Corporation in an out-of-court settlement, the defendant went on to complete the acquisition of the land which had increased significantly in value during the interim period.

The plaintiff argued that over the course of the initial discussions with the defendant the parties had agreed that the plaintiff would contribute not only to the legal costs associated with the claim against the land, but that together they would proceed with a property development plan for the land. This was to include the actual purchase of the land on a joint venture basis. However the defendant argued that there was, at most, an agreement in principle to share costs and any fees paid by the third party vendor in respect of any claim over the land, but that the agreement never involved the land itself.

The decision

The court found that the plaintiff had failed to establish on the balance of probabilities that a binding oral agreement existed in relation to the actual purchase of the land.

In considering whether a fiduciary relationship existed on the facts, the court cited *Chirnside v Fay*² in support of a finding that a fiduciary relationship can exist in a commercial joint venture without the need for the parties to have entered into a joint venture agreement. In *Chirnside*, the Supreme Court held the view that most joint venture relationships can properly be regarded as inherently fiduciary because of their analogy with partnership law. Generally such parties join together in a venture with a view of sharing the profits obtained, and the mere fact that the parties expect to reach a more formal agreement later does not alter the relationship already in existence. In reaching that finding, the Supreme Court considered that "loyalty" was a key feature of the fiduciary relationship formed.

However the court noted that unlike the parties relationship in *Chirnside*, in this instance the defendant's relationship with the plaintiff could only be characterised as one of financial convenience and did not involve any mutuality.

¹ *Tonys Britannia Limited v Interplex at Albany Limited*, High Court Auckland, 8 January 2007, CIV 2005-404-5972

² [2006] 3 NZSC 68

While the court acknowledged that the parties had general respect and trust in each other arising from their past commercial dealings, the court did not find any particular or additional relationship in relation to the land which gave rise to specific duties of loyalty and good faith.

Commercial business law

Government is considering whether to join the 1994 WTO Government Procurement Agreement

The Ministry of Economic Development is calling for business input into whether New Zealand businesses are currently encountering discriminatory access barriers in overseas government markets. Accession to the WTO Government Procurement Agreement is seen as being of particular value to New Zealand exporters in high-tech sectors.

As a result of recent interest shown by a number of firms and business groups in the possibility of improved access into government procurement markets, the Ministry of Economic Development (MED), in conjunction with the Ministry of Foreign Affairs and Trade, is currently undertaking a review of whether New Zealand should join the World Trade Organisation (WTO) plurilateral Government Procurement Agreement (WTO GPA).

At present, although not a member of the WTO GPA, New Zealand maintains an open government procurement market. The WTO GPA does not require discrimination against non-members and in theory, New Zealand exporters already have access to the procurement markets of many of the Agreement's members. Some WTO GPA members however maintain access restrictions which would be eased for New Zealand exporters if New Zealand was to join the GPA. These include Canada, Israel, South Korea, Switzerland, and the USA.

MED notes that in assessing the case for joining the WTO GPA, the benefits of any new access for New Zealand exporters to government procurement markets will need to be weighed mainly against any costs in New Zealand's domestic procurement regime resulting from adoption of the prescriptive GPA procedures.

The WTO GPA is designed to make laws, regulations, procedures, and practices regarding government procurement covered by the Agreement more transparent, and to ensure they do not protect domestic industry or discriminate against products or suppliers from other members. It does this through the mandatory imposition (and enforcement) of a regimented government procurement regime into the domestic system of its members. MED notes that this could lead to the following effects on New Zealand's public sector:

- the possibility of reduced discretion and increased administrative burden arising from the detailed procedural requirements prescribed in the Agreement;
- more complex and protracted tendering and contract award processes may in turn increase costs for suppliers to Government;
- the possibility of sanctions if procurement decisions are challenged under the WTO GPA's formal dispute settlement provisions may increase risk aversion and reduce receptiveness to innovative proposals from industry.

Submissions on the discussion documents for industry and public sector stakeholders closed on 9 February 2007.

For more information and to access the discussion documents released as part of the 2006/2007 New Zealand Government Review of the 1994 World Trade Organisation Agreement on Government Procurement visit MED's website at: www.med.govt.nz.

Company law

Latest leaky building decision: wake-up call for directors and officers

Christine Meechan, a partner in Bell Gully's Litigation department, discusses the recent leaky building case and the controversial finding of personal liability on the part of the director of the insolvent construction company.

Amalgamations and the effect on contracts with third parties

Companies wishing to amalgamate have a choice of two routes under the Companies Act. A recent decision confirms that whether an amalgamation is approved by the court under Part 15 or an amalgamation is effected under Part 13 of the Act, the legal consequences are the same.

"Major Transactions": a fettered fetter?

In this article the author sets out to demonstrate how recent judicial interpretation of the scope of the major transaction provision in section 129 of the Companies Act may substantially reduce the provision's effectiveness as a check on a board's management power.

Company law

Latest leaky building decision: wake-up call for directors and officers

Christine Meechan, a partner in Bell Gully's Litigation department, discusses the recent leaky building case and the controversial finding of personal liability on the part of the director of the insolvent construction company.*

Litigation over defective buildings is nothing new. Much of the case law in the recent high profile High Court leaky building decision comes from the slew of cases over defective foundations which occupied court attention in the 1970s and 1980s.

The recent case of *Dicks v Hobson Swan Construction Ltd*³ is significant, however, as it is one of the first of the leaky building cases to proceed to trial.

Justice Baragwanath's decision represents a comprehensive win for the homeowner, Mrs Dicks, who has been awarded just over \$200,000 in damages. It represents a predictable loss for the local authority, the Waitakere City Council, and an unexpected and no doubt unwelcome finding of personal liability on the part of the director of the insolvent construction company.

The background facts

Mrs Dicks contracted with Hobson Swan Construction Ltd to buy a piece of land in Hobsonville on which construction of a stucco house had begun in 1994.

Mr McDonald, on behalf of Hobson Swan Construction Ltd, had applied for a building consent which had been duly issued by the Waitakere City Council operating under the then relatively new regime created by the Building Act and the Building Code.

The judgment is critical of the council's approach to the consent and inspection process - the application for building consent was apparently for a weatherboard home but in fact the house erected was a stucco clad structure. This was not picked up by the council in any of its inspections, nor was the lack of effective seals at critical junctions between the plaster stucco and other elements of the building such as the windows and doors. This absence of seals was the primary cause of water ingress.

The Waitakere City Council maintained that in approving and granting such a flawed application for consent, it observed the same standard of care as other local authorities at the time. The council's case was that its standards may not have been high, but they were certainly no lower than other local authorities.

This did not impress Justice Baragwanath who effectively found that the Waitakere City Council was responsible for 20% of Mrs Dicks' claim.

However, the problem for the council is that Hobson Swan Construction Ltd, the first defendant against whom findings of fault were also made, is in liquidation and Mr McDonald is similarly impecunious.

This means that although a 20% finding of liability specific to the council was made, it will end up carrying the whole of the judgment of \$200,000 as the other two liable parties cannot meet their share of the judgment. This is the result of the court finding that the company, Mr McDonald and the council were all joint tortfeasors who have joint and several liability to Mrs Dicks.

³ (Unreported, HC Auckland, Baragwanath J, CIV 2004-404-1065, 22 December)

Personal liability of Mr McDonald

Perhaps the most controversial aspect of the case is the finding of personal liability against Mr McDonald. Mr McDonald was a director of Hobson Swan Construction Ltd and it was he who physically performed the construction work on the house throughout 1994.

Mrs Dicks' contract was with the company rather than with Mr McDonald personally. There is a well established principle of law, discussed by the Court of Appeal in *Trevor Ivory v Anderson* in 1992 that even when the company is a "one man band" the natural person that sits behind the corporate veil will not normally be personally liable.

Justice Baragwanath spent a considerable part of his decision assessing the pros and cons of lifting the corporate veil and exposing the individual wrongdoer to personal liability. He concluded that because of the exclusive level of control which Mr McDonald exercised over the construction project, i.e. he was actually the man on the job, he should be personally liable as well as having his negligence attributed to the company.

While recognising a number of factors which told against the imposition of personal liability, Justice Baragwanath concluded:

"Mr McDonald did not merely direct but actually performed the construction of the house and was personally responsible for the omission of the seals."

What can directors do to avoid findings of personal liability?

The key factor in Justice Baragwanath's findings of personal liability was the level of control and hands-on involvement which Mr McDonald had in the construction project. In most large property developments it will be rare for a director to have such a hands-on role, but it would be sensible for any director or officer of a company involved in a development to put as much distance as possible between themselves and the substantive construction, or indeed choices of materials and methods of construction.

Ultimately, there must be a living breathing person, rather than a corporate entity who does physical work of construction and makes choices that affect the quality of the building. On the basis of Justice Baragwanath's analysis, those individuals are exposed to the imposition of the same personal liability sheeted home against Mr McDonald.

The decision represents something of a wake up call for officers and directors involved in the construction industry. Check your insurance policies now!

** Christine Meechan specialises in construction and insurance law. She is currently the President of the New Zealand Insurance Law Association.*

Since this article was written, it has been reported that the Waitakere City Council has decided to appeal this decision on the advice of its insurer, RiskPool.

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Company law

Amalgamations and the effect on contracts with third parties

Companies wishing to amalgamate have a choice of two routes under the Companies Act. A recent decision confirms that whether an amalgamation is approved by the Court under Part 15 or an amalgamation is effected under Part 13 of the Act, the legal consequences are the same.

The background facts

In *Elders New Zealand Limited v PGG Wrightson Limited*⁴, the High Court had to determine whether a court approved amalgamation under Part 15 of the Act had the same legal effect, in relation to the continuing rights and obligations of amalgamating companies, as an amalgamation effected under the standard procedure contained in Part 13 of the Act.

Elders and Wrightson were the co-owners of stock sale yards either in their own names or through certain co-owned companies. The rights and obligations of the parties in relation to the sale yards were regulated by various contractual arrangements and by the constitutions of the co-owned companies. The contractual arrangements and constitutions respectively conferred on the other co-owner a right of pre-emption in respect of the other co-owner's interest in the sale yards. The relevant clause in each instance stated that "[No] party will partition, transfer, sell, lease or otherwise dispose of the whole or part of its interest in the sale yards, except as provided in this agreement" and that pre-emptive rights would arise where a party, "...transfer(s)...or otherwise dispose(s) of the whole or of part of its interest in the Saleyards...".

Subsequently, Wrightson and Pyne Gould Guinness Limited (PGG) agreed to amalgamate pursuant to a "merger" plan that was conditional upon court approval under Part 15 of the Act. That approval was given by the court. Elders formed the view that the application to the court and subsequent approval of the merger plan was a voluntary disposition by Wrightson of its interest in the sale yards, and as such, Elders' pre-emptive rights under the agreements had been triggered.

Elders issued proceedings in the High Court in order to determine whether the court approved amalgamation had the effect of transferring, selling or otherwise disposing of Wrightson's interest in the sale yards. In support of its view, Elders sought to distinguish an amalgamation under Part 13 of the Act, which it considered as occurring by operation of law (that is, upon the issue of a certificate of amalgamation by the Registrar), and an amalgamation under Part 15 of the Act, which it considered was as a result of a consensual agreement of the parties (with court approval being merely a condition precedent to the merger becoming effective).

The court's decision

The court found that the legal effect of an amalgamation was the same under both Parts 13 and 15 of the Act. The Court based its finding on *Carter Holt Harvey Limited v McKernan*⁵. In *Carter Holt*, the Court of Appeal held that amalgamations effected under Part 13 of the Act do not involve the vesting of the rights and obligations of the amalgamating companies by operation of law in a new entity, but rather involve the process of the companies (participating in an amalgamation) continuing in existence as part of the new amalgamated entity.

Applying *Carter Holt*, the High Court held that the old Wrightson continued as part of PGG Wrightson after the merger, even though the old Wrightson had been struck off the register of companies. As Wrightson's assets and liabilities continued in PGG Wrightson it necessarily followed that Wrightson had not in fact disposed or transferred of any interest in the sale yards. Therefore, the court found that Elders' pre-emptive rights had not been triggered under any agreement between the parties or under the constitution of any of the co-owned companies.

⁴ HC AK CIV 2006-404-1974 [1 December 2006]

⁵ [1998] 3 NZLR 403 (CA)

The court also dismissed Elders' proposition that any order made by the court would only be binding between Wrightson and PGG, and would not be binding on Elders. This, it was argued, would mean that

Elders was still entitled to its pre-emptive rights in respect of the sale yards. The court did not agree stating that if that were the case then it would follow that all other persons dealing with an amalgamated entity would be entitled to act without regard to the amalgamation. This could mean, for example, that a plaintiff could bring proceedings against the old Wrightson entity even though it has subsequently been struck off the register.

Practical consequences

This case confirms that the amalgamated company, whether effected under Part 13 or Part 15 of the Act, continues to enjoy all advantages previously conferred on any of the amalgamated companies and is to continue to have their liabilities. It is not to be treated as a new party or a different party to third party contractual arrangements.

Company law

“Major transactions”: a fettered fetter?”

Trish Keeper, *New Zealand Law Journal*, December 2006, p.406

In this article the author sets out to demonstrate how recent judicial interpretation of the scope of the major transaction provision in section 129 of the Companies Act may substantially reduce the provision's effectiveness as a check on a board's management power.

The board of directors are given wide powers to manage a company, but these are tempered in part by section 129 of the Companies Act 1993 which provides a mechanism for shareholders to be warned if the board proposes to make abrupt and substantial changes to the company in which the shareholders have invested.

Section 129 provides that a company must not enter into a major transaction unless that transaction is either approved by a special shareholders' resolution or is contingent on such approval. Further, where such approval is obtained, any shareholder who voted against the special resolution is entitled to require the company to purchase its shares in accordance with sections 110 to 115 of the Act.

For the purposes of section 129, a major transaction is defined as any transaction that is an acquisition, a disposition or one that has or is likely to have the effect of the company acquiring rights or interests or incurring liabilities, which has a value that is more than half the value of the company assets before the transaction occurs.

In this article, Trish Keeper queries whether section 129 has been undermined by a series of recent cases. In particular she argues that the overall impact of these cases has been to severely diminish the protection afforded by this provision to minority shareholders through:

- confining the interpretation of section 129 to refer to transactions of an individual company rather than a group of companies (thereby allowing subsidiaries to hold and dispose of major assets without requiring the approval of the parent company's shareholders); and
- allowing carefully structured transactions to fall outside the ambit of section 129 to avoid an “abrupt and significant transformation” of a company (through, for example, a staged development plan).

She also argues that it is impossible to derive any clear or coherent theme as to the purpose and operation of the section from these cases.

The author develops her arguments through analysing the decisions of the following three cases:

- *Central Avion Holdings Ltd v Palmerston North City Council*⁶ (which concerned a board decision to extend the runway at Palmerston North Airport through a phased business plan implemented in stages);
- *Flight Trainers Ltd v McGormick*⁷ (where it was held that the issue of a debenture was not a disposition within the meaning of section 129); and
- *Re Fletcher Challenge Forests Ltd*⁸ (which involved a complex series of transactions undertaken by various subsidiaries of Fletcher Challenge Forests Ltd).

⁶ HC, Palmerston North CIV 2003-454-559, 15 June 2006, Goddard J

⁷ (1999) 8 NZCLC 261,998

⁸ (2004) 9 NZCLC 263,447

Securities and capital markets

Update on regulations for new securities law

In late December 2006 Cabinet approved the policy for the regulations which are required for the implementation of the changes to the new securities law. The regulations are currently being drafted and it is expected that they will come into effect by mid-2007.

New Securities law website established

As reported in the Spring 2006 issue of Commercial Quarterly a major new suite of securities legislation was passed in October 2006. The full effect of these changes will not be felt by market participants until later this year as we are still waiting on regulations to come through before some of the key provisions take effect. In the meantime, the Securities Commission has set up a website especially to assist the market in understanding these changes.

Changes to increase the benefits of share purchase plans

Louise Hill, a senior associate in Bell Gully's Corporate team, considers a number of issues associated with share purchase plans including the effect of the proposed Securities (Mutual Recognition of Securities Offerings – Australia) Regulations 2006 (and their Australian counterpart) on these plans and the ability of trustees of employee share schemes to participate in share purchase plans.

Securities Commission too late to seek penalties in Tranz Rail insider trading case

The Court of Appeal has confirmed that the Securities Commission will not be able to seek penalties in the case against former Tranz Rail Director, David Richwhite, and Midavia Rail Investments as the penalties claims are time-barred under the current wording of the legislation.

New amendments to the NZAX Listing Rules

After an extensive consultation and review of the NZAX market, NZX has finalised its amendments to the NZAX Listing Rules. It is expected that the new rules will take effect from mid-March 2007.

Bell Gully authors New Zealand M&A chapter in international publication

Bell Gully partners Andrew Brown and Andrew Abernethy have authored the New Zealand section of the International Comparative Legal Guide to Mergers & Acquisitions 2007, published by the Global Legal Group.

Securities and capital markets

Update on regulations for new securities law

In late December 2006, Cabinet approved the policy for the regulations which are required for the implementation of the changes to the new securities law. The regulations are currently being drafted and it is expected that they will come into effect by mid-2007.

The Ministry of Economic Development (MED) released a discussion document on the Securities Legislation Bill regulations in March 2006 in respect of four areas that require regulations to be passed to bring into effect substantial obligations in the Securities Amendment Act 2006, the Securities Markets Amendment Act 2006, the Takeovers Amendment Act 2006 and the Fair Trading Amendment Act 2006 namely:

- investment advisers and brokers disclosure obligations;
- substantial securities holders disclosure;
- insider trading exemptions; and
- market manipulation exemptions.

Of these initial four areas, it has been confirmed that only three will require regulations at this stage. Cabinet has decided against providing specific exemptions from the insider trading provisions in respect of passive investment instruments such as index funds and exchange-traded funds as was originally envisaged.

Substantial security holders' disclosure

The Cabinet paper confirms that only minor changes are required to the substantial security holders' regulations, largely to ensure that they are consistent with the new substantial provisions in the Securities Markets Amendment Act 2006. In addition regulations are proposed to:

- reduce the burden of providing historical information (in certain circumstances);
- exempt overseas-listed companies from the regime where they are complying with similar requirements in their home jurisdiction and to move an exemption notice for investment management contracts into the main body of regulation;
- redesign the default substantial security holders' form in conjunction with the Securities Commission and NZX; and
- require compulsory electronic filing except in circumstances where electronic filing would unduly delay the filing of the notice, and that, with Ministerial approval, the relevant exchange be able to prescribe the method by which the form must be completed and filed.

Market manipulation

In the March discussion document, MED acknowledged that the breadth of the new market manipulation prohibitions may require regulations exempting certain forms of efficient and desirable market conduct from the operation of the rules. The three exemptions under consideration were:

- market stabilisation following an initial public offering;
- short selling; and
- crossing of trades (where securities are traded between clients of a single exchange participant itself without the orders having first been matched in the order screen).

It has now been confirmed that regulations will exempt all three activities.

Market stabilisation following an offer of securities will be exempted on a similar basis to the Australian approach embodied in the "ASIC Interim Guidance on Market Stabilisation".

Regulations for permissible market stabilisation will cover the following areas:

- size threshold,
- disclosure by the issuer,
- reporting by stabilisation manager or broker,
- mechanics of stabilisation,
- report and record keeping,
- disclosure to the market,
- period of stabilisation and prohibition on refreshing the over-allotment option.

Investment advisers' and brokers' disclosure

Investment advisers' and brokers' disclosure obligations are set out in the Securities Markets Amendment Act 2006. Cabinet has agreed that regulations will be drafted to:

- exempt some classes of investment advice (telephone) and adviser (lawyers and chartered accountants, and advisers isolated from certain relationships) from the full requirements of the Act;
- require disclosure to be concise, clear and effective, with set placement of disclosure, format and style, plain language requirements and set headings;
- clarify that where an adviser is giving general advice on securities, disclosure can be general (e.g. remuneration described within a range) but where advice on set securities is provided, then disclosure will be expected to be more specific; and
- define a bank term deposit as a fixed term deposit with a registered bank.

The MED has noted on its website that the regulations will be passed two to three months prior to their coming into effect to allow time for market participants to become familiar with them and prepare for the changes.

To view a copy of the Cabinet paper on the proposed regulations visit MED's website at www.med.govt.nz.

Previous commentary on this topic by Bell Gully is available on our website in the Spring 2006 issue of Commercial Quarterly at www.bellgully.com

Securities and capital markets

New securities law website established

As reported in the Spring 2006 issue of [Commercial Quarterly](#), a major new suite of securities legislation was passed in October 2006. The full effect of these changes will not be felt by market participants until later this year as we are still waiting on regulations to come through before some of the key provisions take effect. In the meantime, the Securities Commission has set up a website especially to assist investment advisers and market participants in understanding these changes.

The website provides an overview of the following key changes under the new Securities law:

- insider trading;
- substantial security holder disclosure;
- market manipulation;
- investment adviser disclosure; and
- the Securities Commission's new enforcement powers.

News releases, articles and speeches on the new securities law also will be available on the website.

The Securities Commission is preparing a *Guide to New Securities Law* which will be published (and available on the website) when the regulations are finalised.

To access the website visit www.newsecuritieslaw.govt.nz

Securities and capital markets

Changes to increase the benefits of share purchase plans

Louise Hill, a senior associate in Bell Gully's Corporate team, considers a number of issues associated with share purchase plans including the effect of the proposed Securities (Mutual Recognition of Securities Offerings – Australia) Regulations 2006 (and their Australian counterpart) on these plans and the ability of trustees of employee share schemes to participate in share purchase plans.

Share purchase plans are a relatively new concept in New Zealand - while there were some share purchase plans undertaken pursuant to specific exemptions from the Securities Act - the Securities Act (NZX – Share and Unit Purchase Plans) Exemption Notice 2005 was only gazetted in November 2005. Since then, there have only been a handful of share purchase plans undertaken by companies listed on the New Zealand Stock Exchange. However, as companies begin to realise the benefits of undertaking a share purchase plan, this is expected to increase.

Share purchase plans allow a company to issue up to NZ\$5,000 worth of shares (to a maximum of 30% of the shares currently on issue) to existing shareholders utilising a fairly short, simple offer document. The rationale for the Exemption Notice is that a full disclosure document, such as an investment statement, is not necessary given that issuers are subject to the continuous disclosure requirements of the NZX and thus existing shareholders will be fully informed about the company.

As a full disclosure document is not required, share purchase plans are an inexpensive way of raising capital from existing shareholders. Share purchase plans also allow small shareholders to participate in capital raising where they may not otherwise have been able to do so because of the cost to the company of preparing a prospectus or investment statement. For example, both Fisher & Paykel Appliances and Rakon (for whom Bell Gully act) have undertaken or are undertaking share purchase plans in association with a private placement as part of capital raising to fund acquisitions. In these situations share purchase plans enable a shareholder to increase their investment in a company at a time when the company is expanding. Share purchase plans may also be undertaken to provide funds for the general development and expansion of the company. This was the purpose of the ICP Biotechnology share purchase plan, for whom Bell Gully also acts.

This article considers a number of interesting aspects of the share purchase plan and some areas where improvement to the regulation of share purchase plans could be considered, including:

- the effect of the proposed securities (Mutual Recognition of Securities Offerings – Australia) Regulations 2006 and their Australian counterpart on share purchase plans;
- whether the regulations permit employees holding shares through employee share plans to participate in the share purchase plan; and
- the impact of the treatment by NZX of share purchase plans as being a rights offering.

Securities (Mutual Recognition of Securities Offerings – Australia) Regulations 2006

Mutual recognition regimes allow each country to retain their own standards, while removing barriers to trade between them. The mutual recognition of offers of securities scheme allows an issuer to extend an offer that is being lawfully made in one country to investors in the other country without the issuer being required to comply with most of the substantive requirements of the host jurisdiction's fundraising laws that apply to domestic offers.

The proposed regulations give effect to the Trans-Tasman Mutual Recognition of Offers of Securities and Managed Investment Scheme Interests regime. When enacted, these regulations will allow the offer of securities and managed investments to be made by an Australian company in New Zealand using the same offer documents that the company uses in Australia. Similarly, the equivalent Australian legislative amendments, the Corporations Amendments (NZ Closer Economic Relations) Bill 2006, will allow New Zealand companies to offer securities in Australia using the New Zealand offer document.

The mutual recognition scheme aims to overcome mutually inconsistent requirements that may exist between national regulatory frameworks and to reduce compliance costs associated with the need to comply with the different regulatory requirements of different jurisdictions. The proposed scheme is intended to reduce duplicated regulation, and thereby facilitate investment between New Zealand and

Australia, enhance competition in capital markets, reduce costs for business and increase choice for investors. The scheme achieves this by allowing entities from New Zealand to offer securities into Australia on the basis of compliance with the New Zealand fundraising requirements and with minimal additional requirements imposed by Australian law. This is intended to reduce costs significantly for New Zealand issuers, as they will no longer be required to prepare separate documents to comply with Australian regulation, and vice versa.

At present, New Zealand companies must be listed on the NZSX in order to take advantage of the Exemption Notice for share purchase plans. ASIC's present position appears to be (although it is not entirely clear) that New Zealand companies listed on the NZSX but not listed on the ASX may not make an offer under a share purchase plan complying with the Exemption Notice to Australian resident shareholders, without preparing a full disclosure document under the Corporations Act 2001 (Cth). Conversely, Australian companies listed on the ASX but not listed on the NZSX may make an offer under a share purchase plan complying with the Australian Class Order to New Zealand resident shareholders because of the Securities Act (Overseas Listed Issuers) Exemption Notice 2002.

Corporations Amendment (NZ Closer Economic Relations) Bill

The mutual recognition regime may resolve this problem by allowing New Zealand companies listed on the NZSX to offer to Australian resident shareholders utilising a short form offer document that complies with the Exemption Notice.

The Corporations Amendment (NZ Closer Economic Relations) Bill 2006 provides that certain rules (including Chapter 6D other than section 736), do not apply to eligible recognised offers. An offer of securities is a "recognised offer" if the following conditions are met:

- the person proposing to offer the securities must be a person incorporated by or under the law of the recognised jurisdiction (which in this case would be New Zealand) or must fall within one of the other classes of person (such as a natural person resident in New Zealand);
- the person proposing to offer the securities must not be banned under section 1200N;
- the proposed offer must be an offer of a kind prescribed by regulations in relation to the recognised jurisdiction; and
- at least 14 days before the day on which the offer is first made in Australia, the person proposing to make the offer must lodge with ASIC a notice in the prescribed form of the person's intention to make a recognised offer, and the documents and information required to be lodged by section 1200C of the Corporations Act.

Effect of mutual recognition regime on share purchase plans

New Zealand issuers will be permitted to extend an offer under a share purchase plan to shareholders resident in Australia if the offer under the share purchase plan could be considered to be "an offer of a kind prescribed by regulations in relation to the recognised jurisdiction". The regulations have yet to be drafted so it is not yet certain whether a share purchase plan will be prescribed by the regulations. We would expect that the mutual recognition regime should extend to the offer document prepared in relation to a share purchase plan, allowing an entity listed on the NZSX to make its share purchase plan open to Australian resident shareholders, and to provide those shareholders with the same offer document (amended to include the "health warning" required by the Australian legislation) that it provides to its New Zealand shareholders.

Since the rationale for the exemption of share purchase plans from securities legislation requirements applies to shareholders that are resident in both New Zealand and Australia, it makes sense to extend the mutual recognition regime to share purchase plans. In relation to entities listed on the NZSX, Australian shareholders are able to access information in relation to those entities on the NZSX website, and Australian shareholders receive annual reports and other information relating to the NZSX listed issuer. Similarly, New Zealand shareholders can access information on ASX listed entities through the ASX website.

The mutual recognition regime will still not solve problems for companies that are dual listed. There is a slight inconsistency between the New Zealand Exemption Notice and the Australian Class Order relating to the treatment of "custodians". In New Zealand custodians need only give a certification when applying for shares on behalf of beneficial owners, while in Australia custodians must be "noted as such" on the share register in order to make an application on behalf of beneficial owners. Given that both the Exemption Notice and the Class Order require that the offer must be made on the same terms to all shareholders,

companies have to find a way to comply with the requirements of both the Exemption Notice and the Class Order in relation to custodians. Fortunately at least some share registries in New Zealand “code” custodians on the share register, which solved the problem for Fisher & Paykel Appliances in their share purchase plan last year. However if this is not always the case, then it may be that an exemption from the Australian Class Order would be required in order to allow for custodians to acquire shares on behalf of beneficial owners. This would seem to negate somewhat the advantages of the share purchase plan as being a relatively simple, inexpensive capital raising method. Ultimately, it may be that little can be done and the differences are a consequence of the different laws relating to companies in New Zealand and Australia.

Employee share schemes

The definition of “custodian” in the Exemption Notice is not, in general, wide enough to allow trustees of employee share schemes to acquire shares on behalf of the beneficial owners of shares under the employee share schemes. To be a “custodian” for the purposes of the Exemption Notice (and thus be permitted to acquire up to NZ\$5,000 of shares per beneficial owner), a custodian must be one of the following:

- a trustee corporation or nominee company which holds securities by reason only of acting for another person in the ordinary course of business of that trustee corporation or nominee company; or
- a bare trustee holding securities on trust.

Most employee share scheme trustees would not fall within the first limb of this definition, as they are generally not trustee corporations or nominee companies, and do not hold shares as part of the ordinary course of business. Employee share scheme trustees would often not fall within the second limb either, since they generally have some level of discretion in relation to the employee share scheme, thus disqualifying them as bare trustees.

Some companies are disappointed that their employees, holding shares through an employee share scheme, are not permitted to participate in the share purchase plan. We wonder if it would be useful to amend the Exemption Notice to add a third category to the definition of “custodian”, namely trustees of employee share schemes. This would be a very limited category and would allow employees to participate in capital raising of the company they work for.

Rights offering

The NZX treats a share purchase plan as a rights offering, unlike the ASX in Australia. This means that listed issuers must comply with the requirements of NZSX Listing Rule 7.10, which sets out the timing and process requirements for rights offerings. One of these requirements is that the issuer must give ten business days’ notice of the record date, utilising the appendix 7 form.

There are a couple of points we have noticed that flow from this requirement:

- appendix 7 in its present form does not happily “fit” with share purchase plan information, particularly as to the price and number of shares to be issued, as this information is often not known ten business days before the record date. This is a small administrative matter that is easily rectified by the preparation of an amended Appendix 7;
- allowing ten business days’ notice may have the unintended effect of encouraging the public to acquire a small number of shares, in order to make them eligible to participate in the share purchase plan, under which they are offered shares at a discount to average end of day market price over a specified period. This is not the purpose of the share purchase plan; it is not to encourage people to buy 100 shares so that they may subsequently acquire up to NZ\$5,000 at a discount. This potential effect is an unfortunate consequence of the requirement to notify the record date ten business days’ in advance. If it proves to be a material issue, the notice period for the record date could be reduced and the period for which the offer is required to be open could be extended. Any amendment to the notice period should still allow custodians to undertake all necessary processes to obtain instructions from their beneficial owners.

Conclusion

The share and unit purchase plan scheme benefits both issuers and their shareholders by providing an inexpensive and relatively simple capital raising method. Issuers and their shareholders will benefit further when NZSX listed issuers are permitted to offer to Australian registered shareholders under share purchase

plans. Some small tweaks are however required to strengthen the scheme, including, in particular, by allowing employee share schemes to participate.

Securities and capital markets

Securities Commission too late to seek penalties in Tranz Rail insider trading case

The Court of Appeal has confirmed that the Securities Commission will not be able to seek penalties in the case against former Tranz Rail Director, David Richwhite, and Midavia Rail Investments as the penalties claims are time-barred under the current wording of the legislation.

Background

The Securities Commission commenced proceedings in October 2004 seeking compensation and statutory penalties against six parties who were alleged to have been involved in insider trading in February 2002 in shares held in Tranz Rail Holdings Limited (now Toll NZ Limited). Four of the original six defendants have since settled with the Commission.

In a preliminary application, the court was asked to determine whether the Commission was entitled to seek statutory penalties as well as compensation against the defendants. The High Court⁹ determined that it was not entitled to do so as the Commission's causes of action under section 7 (for insider trading) and section 9 (for tipping) of the Securities Markets Act (the Act) accrued when the alleged insiders sold their shares and thereby "avoided losses". Given that the trades in question occurred in February 2002 this meant that the Commission was time-barred from recovering penalties by the two year limitation period "from the date on which the cause of action accrued" prescribed under the Limitation Act.

The Commission appealed this decision on the basis that:

- whilst it agreed with Williams J's finding that the loss avoided as a result of the insider trading was an element in the cause of action, the Commission was of the view that no loss or gain in fact occurred unless and until the inside information became publicly available. Since this was "an unresolved issue of fact", the Commission argued that the matter should be left for consideration by the trial judge; in the alternative
- the Commission argued that the doctrine of reasonable discoverability should apply to the causes of action and that since this required "factual evaluation" the claim should be allowed to proceed to trial.

Court of Appeal's decision

The Court of Appeal¹⁰ rejected both of the Commission's arguments. In reaching its decision, the court agreed with the respondents' argument that a loss or gain was not an element of the causes of action for the insider trading and tipping. In its view, the causes of action under sections 7 and 9 of the Act were complete when the trades took place. Accordingly, the court held that the Commission was time-barred from pursuing penalties against the respondents.

Position under new insider trading regime

It should be noted that when the new insider trading regime (passed in October last year) comes into force this will no longer be the position. Under the new regime, the Securities Commission will be able to bring an application for a pecuniary penalty at any time within three years after the date on which the matter giving rise to a contravention of the insider trading provisions "was discovered or ought reasonably to have been discovered."

⁹ *Securities Commission v Midavia Rail Investments BVBA* (Unreported, High Court AK CIV 2004-485-2174, 28 September 2005 and 13 January 2006)

¹⁰ *Securities Commission v Midavia Rail Investments BVBA and Ors* (Unreported, Court of Appeal, CA252/05, 29 November 2006)

Securities Commission's position

The Securities Commission has indicated¹¹ since that it does not intend to appeal this decision but will continue to pursue its claim for compensation against the two remaining defendants.

Bell Gully is acting for the two remaining defendants, David Richwhite and Midavia Rail Investments.

¹¹ The Bulletin, (The Quarterly Newsletter of the New Zealand Securities Commission) No. 38, January 2007, p.1

Securities and capital markets

New amendments to the NZAX listing rules

After an extensive consultation and review of the NZAX market, NZX has finalised its amendments to the NZAX listing rules. It is expected that the new rules will take effect from mid-March 2007.

The amendments to the NZAX listing rules were originally due to be implemented at the same time as the NZSX/NZDX listing rules in May last year (since they were to replicate the relevant NZSX listing rule changes). However, subsequently it was decided that any changes to the NZAX listing rules should be postponed until after a separate review of the NZAX market was completed. The review was completed in August 2006.

The review of the NZAX market in relation to the listing rules had two key findings:

- relatively few NZAX listed issuers had a clear understanding of the distinctions between the NZAX listing rules and the NZSX listing rules; and
- market participants did not consider any major rule changes to be necessary.

Consequently, NZX has proceeded with amending the rules to reflect the changes already made to the NZSX listing rules in May 2006 but, to assist market participants in distinguishing the difference between the two sets of rules, NZX has also reordered the NZAX Listing rules to follow the structure of the NZSX listing rules. A comparative [chart](#) of these changes is available on NZX's website at www.nzx.com.

NZX has also made two further changes to the NZAX Rules by omitting the existing NZAX provisions dealing with unit trusts and equity warrants.

To access a copy of the amendments to the NZAX listing rules visit NZX's website at www.nzx.com/regulation.

The Bell Gully [Guide](#) on the 2006 NZSX Listing Rule amendments is available on our website.

Securities and capital markets

Bell Gully authors New Zealand M&A chapter in international publication

Bell Gully partners Andrew Brown and Andrew Abernethy have authored the New Zealand section of the International Comparative Legal Guide to Mergers & Acquisitions 2007, published by the Global Legal Group.

The New Zealand chapter includes relevant information about New Zealand authorities and legislation, the mechanics of acquisition, stakebuilding, deal protection and bidder protection.

You can read the New Zealand chapter [here](#) or visit the Bell Gully website news section.

This chapter was first published in the Global Legal Group Ltd International Comparative Legal Guide to Mergers & Acquisitions 2007 and is reproduced with the permission of the publisher www.iclg.co.uk.

Competition and consumer law

Unresolved issues in price fixing: market division, the meaning of control and characterisation

In this issue we review a recent article which considers how pro-competitive arrangements that could technically amount to “price fixing” should be assessed.

Competition and consumer law

Unresolved issues in price fixing: market division, the meaning of control and characterisation

Paul Scott, Canterbury Law Review, Volume 12, November 2006, p.197

In this issue we review a recent article which considers how pro-competitive arrangements that could technically amount to "price fixing" should be assessed.

Regulators worldwide aggressively target "cartel" behaviour such as price fixing. However, not all price fixing takes the form of simple agreements between competitors on price, and seemingly innocuous conduct can sometimes be caught. Often such conduct forms part of a broader series of otherwise legitimate arrangements such as joint ventures.

This article looks at how such conduct should properly be assessed. The issue is relevant because if conduct amounts to price fixing then (unless the parties seek and obtain a formal "authorisation" from the Commerce Commission), the conduct is per se illegal - it doesn't matter if it has no impact on competition, or even if it has a pro-competitive effect.

The author argues the price fixing prohibition aims to prohibit "hard core cartels", not efficiency enhancing conduct and that where an overly strict interpretation might give rise to liability for pro-competitive arrangements, the New Zealand courts should engage in "characterisation". This involves asking whether the arrangement resulted in a pro-competitive outcome, and if so, whether the particular aspects in question were integral to obtaining that outcome.

While this article does not explore in detail when the joint venture exemption for price fixing is available, it is worth reiterating the exemption does provide protection from price fixing for properly structured joint ventures, albeit in more limited circumstances than many might expect.

Intellectual property and information technology

The colour yellow – brand or not?

A recent decision confirms that a high level of factual distinctiveness will be required before a single colour can be registered as a trade mark in New Zealand.

The importance of pleadings in copyright infringement cases

A recent New Zealand Supreme Court decision provides a very useful reminder of the importance of correct pleadings in copyright infringement proceedings. This necessarily involves clear and accurate identification of the copyright work.

An overhaul of the 1994 Copyright Act is underway

The Copyright (New Technologies and Performers' Rights) Amendment Bill passed its first reading in Parliament in December 2006 and is currently before the Commerce Select Committee. Submissions on the Bill are due by 9 March 2007. In this commentary Bell Gully partner Wayne Hudson outlines the key changes proposed by the Bill.

Intellectual property and information technology

The colour yellow – brand or not?

A recent decision confirms that a high level of factual distinctiveness will be required before a single colour can be registered as a trade mark in New Zealand.

Background

The trade mark registration for the colour yellow held by Telecom IP Limited in New Zealand has been the subject of a recent decision by the Commissioner of Trade Marks. The decision was the culmination of an application made by Cabbage Tree Press Limited for the expungement of the colour yellow registration from the Register of Trade Marks on the grounds that the trade mark was entered on the Register without sufficient cause as it did not meet the requirements for registrability under the Trade Marks Act 1953 (the registration was filed in 1999 and therefore governed by the Trade Marks Act 1953 rather than the current 2002 Act). It was argued by Cabbage Tree Press Limited that the colour yellow was not distinctive and therefore should not have been registered as a trade mark.

The registration under attack was made in respect of "*electronic telephone directory services enabling users to access business information.*"

The decision

Whilst the registration of a colour or colours is specifically allowed under the Trade Marks legislation in New Zealand, the decision of the Commissioner to order the expungement of the registration highlights the difficulty in establishing that single colour trade marks actually function as trade marks or badges of origin as opposed to merely being colours associated with a business or associated with a brand image - the latter not being sufficient to justify registration.

Despite the almost iconic status of the Yellow Pages directories of Telecom in the New Zealand market, the Commissioner of Trade Marks considered that Telecom had not satisfied the onus of establishing that the colour yellow itself had been used as a trade mark or a badge of origin for the services in question despite being an important part of the Telecom brand image.

Practical consequences

The decision offers up some very practical issues to be considered by brand owners who may be contemplating seeking registration of colour trade marks.

Telecom had used different shades of yellow and specifically had not restricted use to the particular Pantone shade which was the subject of the trade mark registration in question. Furthermore there had been no consistent use of the colour – sometimes it had been used as a background colour, sometimes used to highlight headings and other times used for text. This inconsistent use of the colour did not assist Telecom's argument that the colour yellow was being used as a trade mark or badge of origin.

Furthermore, Telecom could offer no evidence that it had specifically promoted the colour yellow as a trade mark.

Although the Commissioner of Trade Marks accepted that the colour yellow had been used by Telecom over a number of years on the hard copy Yellow Pages directory of which there had been significant sales, as well as used for the Internet version of the Yellow Pages directory of which there were many users, this on its own was not sufficient to constitute evidence that the colour yellow was distinctive in relation to these services. The need for very specific evidence of distinctiveness was not met.

The case establishes that evidence of distinctiveness in relation to single colour marks requires more than simply filing evidence of long and extensive use of the colour in relation to the business. A brand owner must be in a position to demonstrate that the colour itself has been promoted as a brand and used extensively so that it is recognised in the marketplace as a badge of origin for the goods or services in question. Telecom could not prove that the public would expect that the electronic directory services were linked with Telecom because they were offered by reference to the colour yellow.

Another factor which weighed against Telecom was the fact that it had invariably used the colour yellow in conjunction with one or more of its other prominent trade marks, such as the words YELLOW PAGES and the well known Walking Fingers logo. This made it difficult to argue that the colour alone was operating as a brand (this may be a significant hurdle for many brand owners).

Clearly any brand owner contemplating registration of a single colour trade mark needs to be in a position to demonstrate consistent use of the same shade of the colour as is the subject of the anticipated application for registration. There needs to be a consistent usage of the colour and promotion of the colour in its own right as a brand. Furthermore, linking the colour to other brands - particularly word or logo brands, will give rise to a question as to whether the distinctiveness relates to those other brands rather than merely to the colour itself – highlighting the need for direct evidence that the colour is recognised as a badge of origin in the marketplace.

It remains to be seen whether Telecom will appeal this decision.

Advice and information

This article is by Bell Gully senior associate, [Colleen Cavanagh](#). Bell Gully's [Intellectual Property team](#) can advise you on all types of IP issues, including the registration and maintenance of trade marks. Contact the team for more information.

Intellectual property and information technology

The importance of pleadings in copyright infringement cases

A recent New Zealand Supreme Court decision provides a very useful reminder of the importance of correct pleadings in copyright infringement proceedings. This necessarily involves clear and accurate identification of the copyright work.

In the case of *Henkel KGAA v Holdfast New Zealand Limited*¹², the appellant (Henkel) claimed that the respondent (Holdfast) had infringed its copyright in the design for Henkel's SuperAttak adhesive packaging when Holdfast designed the packaging for its UltraBonder adhesive. The packaging comprised a multi-coloured card on which the bottle of adhesive was contained in a clear plastic blister pack.

In the High Court Henkel's claim was upheld but Holdfast was successful on appeal to the Court of Appeal in having the declaration and injunction made in Henkel's favour set aside. In this proceeding Henkel appealed to the Supreme Court seeking to restore the Orders made in the High Court.

Background

By way of background Holdfast admitted to having obtained a sample of Henkel's SuperAttak adhesive packaging and to copying this packaging for an adhesive product which Holdfast called SuperBonder. Henkel issued proceedings for copyright infringement and Holdfast agreed to cease using the copied packaging. Holdfast redesigned its packaging and renamed its product UltraBonder. Henkel maintained that the new Holdfast UltraBonder packaging was still an infringement of copyright in the drawing which underlay its SuperAttak product packaging.

Before the Supreme Court could examine the substantive issue of copyright infringement it was required to deal with a claim by Holdfast that Henkel could not rely on its drawings for its SuperAttak adhesive product. In this case the Supreme Court agreed with Holdfast's argument.

In the first instance trial in the High Court Henkel had stated that it sold adhesives, including SuperBonder and Loctite in packaging consisting of a card and blister packaging incorporating what it called the "Blue Image Design". There was a description of 20 separate features of the so called Blue Image Design. The separately identified features were held by the Supreme Court to be common to Henkel's package generally and not to point clearly to the SuperAttak product. Nor were these particulars descriptive of the so called Cupidue drawing which was identified as the drawing on which Henkel's SuperAttak product packaging was based.

Supreme Court's decision

The Supreme Court commented that nowhere in the relevant part of the Statement of Claim as a whole was there any reference to the Cupidue drawing and that the implicit reference to drawings was limited to drawings which underlay the packaging for Henkel's SuperBonder and QuickTite products. The court concluded therefore that at best it was only those artistic works which could be relied on and not on a drawing or drawings which underlay the packaging for Henkel's product known as SuperAttak.

This decision highlights the need for statements of claim not to merely show the general nature of the claim but to give sufficient particulars to inform the court, and the party against whom relief is sought, of the plaintiff's cause of action. In a case of copyright infringement this necessarily involves clear and accurate identification of the copyright work which the defendant is said to have infringed. In the present case Henkel's failure to plead the copyright work on which it ultimately sought to rely resulted in its inability to rely on that work and accordingly Henkel's appeal to the Supreme Court was dismissed.

Additional comments on substantive claim

Although the decision on the pleadings determined these appeal proceedings, the Supreme Court took the opportunity to comment on the substantive copyright claim.

¹² [2006] NZSC 102

The court considered that to succeed in an action for breach of copyright the plaintiff has to establish two things:

- that it is the owner of a copyright work; and
- that the defendant has infringed that work.

Identifying copyright work

On the issue of ownership of copyright the court stated that the plaintiff must clearly and accurately identify the copyright work or works in respect of which it is claiming infringement. This case was held to concern the sub-category of artistic works which is defined in section 14(1) of the Copyright Act 1994 as including a graphic work. The court held that this was the type of artistic work within which the design drawing for the packaging would be included.

Work must be original

The court went on to say that once the plaintiff has identified the work for which it is claiming copyright, it must next establish that the work is an original work although there need be nothing novel in a work for it to qualify for copyright protection. To be original for copyright purposes the work must originate from its author and be the product of more than minimal skill and labour. The court commented that in general terms the greater the originality the wider the scope of protection will be under Copyright law. In this case Henkel had to identify and prove that it had copyright in the graphic work from which it had derived the packaging said to have been copied by Holdfast and to prove that that work was original. Had it been open to Henkel to make this argument based on the pleadings, Henkel would have had to prove that the Cipidue or other drawing(s) which underlay its SuperAttak packaging was an original graphic work and that it had ownership of the copyright work. The court commented that this was a case which involved copyright deriving from a collocation or arrangement of features not original in themselves. A graphic work could qualify for copyright protection because its originality lies in the way in which a number of features, which may have no originality in themselves, have been arranged or collocated.

Infringement

The court then went on to consider the second issue as to whether there had been infringement and stated that this can be usefully considered under two sub-headings:

- (a) Proof of copying, and
- (b) substantial part.

The court stated that proof of copying will seldom be direct and in most cases the court will rely on inference. Clearly the closer the similarity between the two works the stronger the inference that one was copied from another. Access to the copyright work and opportunity to copy by the infringer will also be taken into account subject to any evidence there may be that no copying actually took place.

On the issue of substantial part, the court commented that it was not necessary for a plaintiff to show that the defendant had copied the whole of the work or that the copying was exact. It would be enough if the plaintiff demonstrated that the defendant copied a substantial part of the copyright work. The court relied on the statement made by Justice Gault in *Blenheim v. News Media (Auckland) Limited*¹³ that what must have been copied is the essence of the copyright work.

Outcome

On the facts of the case in question, assuming Henkel had pleaded the Cipidue drawing underlying its SuperAttak packaging, the court stated that it would have had no difficulty in holding that Henkel owned copyright in that work as it was made by a combination of its employees and Cipidue on its commission. Furthermore, the work clearly had sufficient skill and labour going into the arrangement of, admittedly unoriginal, features to qualify the work for copyright protection.

The next question therefore was whether Holdfast had indirectly copied Henkel's copyright work when it produced its UltraBonder packaging. The Supreme Court considered the correct approach was to contrast Henkel's SuperAttak drawing and Holdfast's UltraBonder packaging. They commented that a number of

¹³ [1994] 2 NZLR 673 at p678

the features of Holdfast's UltraBonder packaging bore as much resemblance to its own earlier packaging as to Henkel's arrangement of features in its SuperAttak packaging. The court concluded that there were sufficient dissimilarities between the packaging that they did not consider that Holdfast's UltraBonder packaging indirectly copied a substantial part of Henkel's SuperAttak drawing and that Holdfast's packaging could not be said to be a copy of the substantial part of Henkel's work.

Accordingly, the Supreme Court did not consider infringement would have been established even if Henkel had been entitled to rely on the drawings lying behind its SuperAttak product packaging.

Advice and information

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Intellectual property and information technology

An overhaul of the 1994 Copyright Act is underway

The Copyright (New Technologies and Performers' Rights) Amendment Bill passed its first reading in Parliament in December 2006 and is currently before the Commerce Select Committee. Submissions on the Bill are due by 9 March 2007. In this commentary Bell Gully Partner [Wayne Hudson](#) outlines the key changes proposed by the Bill.

The Bill seeks to bring New Zealand's copyright law up-to-date with digital technology and make it more consistent with those of our major trading partners. The amendments introduced by the Bill aim to reduce the need for costly litigation and piracy by clarifying what constitutes copyright infringement. If the Bill is passed, the amendments will be reviewed within five years to ensure that they operate effectively.

Key changes and issues

Copying and communication

The Bill amends the definition of "copying" to make it clear that in the Copyright Act 1994 it includes the copying of works in any digital format.

The definition of "copying" includes the unavoidable and inconsequential copying processes that occurs when people browse the internet. Transient or incidental copying will not constitute an infringement of copyright, as long as it is a necessary part of a technological process and has no independent economic significance. This exception applies to transient copying of both recorded works and performances.

To keep up with technological developments, the Bill replaces references to "broadcast" and "cable programme" with the technology-neutral expression "communication work", which is defined as:

"a transmission, or the making available by a communication technology, of sounds, visual images, or other information, or a combination of any of those, for reception by members of the public, and includes a broadcast or a cable programme".

In line with this change, the Bill replaces the copyright holder's right to "broadcast the work or include the work in a cable programme service" with a technology-neutral right to "communicate the work to the public".

Under the Act, a cable programme service can receive and re-transmit broadcasts without infringing the original broadcaster's copyright. The Bill will repeal this section.

Changes relevant to educational establishments

The Bill allows educational establishments to make and store digital copies of copyright works without infringing copyright, subject to the following conditions:

- digital copies can only be supplied to students of the establishment having lessons relating to the particular work;
- digital copies can be stored by an educational establishment if specified information is attached to the material and use of the material is restricted to students participating in the course for which the material is stored; and
- the educational establishment must delete the material within a reasonable timeframe once it is no longer relevant to the course for which it was stored.

Changes relevant to libraries and archives

The Bill allows a library or archive to give users on-site and off-site access to works in digital formats without infringing copyright. The library or archive must inform the user in writing about limits on copying and communication of the work prescribed by the Act, and ensure that the digital copy cannot be altered or erased by the user. A library or archive can supply a digital copy of a work to a user, or to another library or archive, provided specified conditions are met.

Computer programs

The Bill allows the lawful user of a computer program, expressed in a low level language, to decompile the program without infringing copyright if certain conditions are met. In particular, decompilation must be necessary to the objective of creating an independent program that is not substantially similar in expression to the decompiled program. Further, the information obtained from decompilation must not be used for any other purpose nor passed on to any other person.

Lawful users of computer programs may copy or adapt a program without infringing copyright where doing so is necessary for their lawful use of the program, (for example, correcting an error in the program). However, a user may only copy or adapt a program to correct an error if a properly functioning and error-free copy of the program is not available within a reasonable timeframe at the ordinary commercial price.

Under the Bill, contractual terms or conditions relating to the use of a computer program have no effect if they aim to prohibit decompiling, copying or adapting a program in accordance with the conditions set out for those activities. Contractual terms or conditions are also invalid if they aim to prohibit a user from studying the functioning of a program to understand the underlying ideas and principles.

Copying sound recordings for private and domestic use

The Bill allows for the widespread practice of copying music into different formats for use with different devices. It allows individuals to copy sound recordings into different formats without infringing copyright if the following conditions are met:

- the sound recording to be copied is not itself an infringing copy; and
- the person making the copy owns the original sound recording, and acquired it legitimately; and
- the copy is for the owner's private and domestic use only; and
- only one copy for each type of playing device owned by the owner can be lawfully made; and
- the owner of the sound recording retains ownership of any copies made.

If the owner is bound by any contract specifying the circumstances in which a sound recording can be copied, the contract would override the conditions set out in the Bill.

This section of the Bill is limited to sound recordings. It does not allow for the copying of audiovisual works such as movies and music video clips into different formats. Practices such as copying CDs for friends and online file sharing would therefore remain an infringement of copyright.

This section of the Bill expires two years after it comes into force, unless the Governor General extends it.

Liability of internet service providers (ISPs) for infringement of copyright

Copying material is an essential part of many services provided by ISPs. Under the Copyright Act, ISPs could potentially face liability for primary and secondary copyright infringement. The Bill does limit ISP liability in some circumstances and in order to qualify for the limitations, an ISP must implement a policy of terminating the accounts of repeat copyright infringers.

An ISP will not be criminally or civilly liable for copyright infringement by a user of the ISP's services. An ISP will not infringe copyright by storing infringing material provided by a user unless it knew or had reason to believe that the material infringed copyright in a work, and failed to delete or prevent access to the infringing material as soon as possible after acquiring such knowledge.

An ISP will also be liable for copyright infringement if the user is "acting under the authority and control" of the ISP. If an ISP deletes a user's material or blocks access because of suspected copyright infringement, the ISP must notify the user of its actions.

An ISP will not infringe copyright by caching infringing material where the ISP:

- does not modify the material; and
- complies with any conditions imposed by the copyright owner; and

- does not interfere with the lawful use of technology to obtain data on the use of the material; and
- updates the material in accordance with industry practice.

If an ISP becomes aware that material it has cached has been blocked or deleted at its original source, it must delete or block access to the cached material as soon as possible. Failure to do so will constitute a copyright infringement.

The copyright owner will still have the right to seek an injunction against the ISP.

Clarification relating to technological protection measures (TPM)

A TPM is a mechanism or system that prevents or inhibits copyright infringement, for example the anti-copying technology now commonly used on music CDs. Devices and means for overcoming TPMs, known as TPM spoiling devices, have been developed.

The Bill prohibits making a TPM spoiling device available for sale or hire, and prohibits actions leading to a TPM spoiling device becoming available for sale or hire, such as making or importing one. Providing a service or information intended to enable or assist others to circumvent a TPM is also prohibited. These prohibitions only apply where the person providing the TPM spoiling device, service, or information, knows or has reason to believe that it would be used to infringe copyright in a TPM-protected work. A breach of these prohibitions is an offence with a penalty of a fine up to \$150,000, up to five years imprisonment, or both.

It should be noted that the act of circumventing a TPM itself is not expressly prohibited.

Libraries, archives and educational establishments may use TPM spoiling devices to overcome TPMs in order to carry out permitted copying, correct errors in computer programs, effect interoperability of software and undertake encryption research.

If someone wishes to copy a CD into MP3 format for their MP3 player, but is prevented from doing so by a TPM, they must approach the copyright owner for assistance. If this is unsuccessful they could engage a librarian or archivist to use a TPM spoiling device to overcome the TPM on their behalf.

Copyright management information (CMI)

Copyright management information (CMI) is information attached to a copyright work that identifies the author or copyright owner of the work, or indicates terms and conditions for use of the work. The Bill prohibits interference with CMI without the authorisation of the copyright owner if the interfering person has reason to believe that the interference would induce, enable or conceal copyright infringement.

The Bill creates an offence for commercial dealing of a work with knowledge that its CMI has been interfered with, without the authorisation of the copyright owner, and knowledge that dealing will induce, enable, or conceal, a copyright infringement. The offence carries a penalty of a fine up to \$150,000, up to five years imprisonment, or both.

To access a copy of the Copyright (New Technologies and Performers' Rights) Amendment Bill visit Parliament's website at www.parliament.nz.

Utilities and resources

Telecommunications Amendment Bill makes its final assent

New Zealand is in line for significant changes in its telecommunication industry following the passage of the Telecommunications Amendment Bill late last year. In this commentary, Bell Gully senior solicitor David Blacktop provides a brief overview of the key provisions of the new legislation.

A look back over oil and gas litigation in 2006

In this article Bell Gully senior associate David Coull reviews three cases involving New Zealand's oil and gas legislative regime each of which provide important lessons for lawyers and industry participants.

Draft New Zealand Energy Strategy released in December 2006

The Energy Strategy, entitled "Powering our Future - Towards a sustainable low emissions energy system", sets out the Government's strategic vision for New Zealand's energy system until 2050. It is a relatively comprehensive document, and refers to several other related policy initiatives (including those relating to climate change and energy efficiency). This commentary outlines the Government's key objectives and proposals put forward for consideration in the Energy Strategy.

Climate change and sustainable land management

At the end of 2006 the Government released a series of related discussion documents on the energy sector and climate change. These include a paper on the Government's proposed plan of action for the forestry and agricultural sectors with particular emphasis on the way forward for a carbon neutral economy and way of life.

Electricity lines company fails in its attempt to get price thresholds set aside

David Blacktop, a senior solicitor in Bell Gully's competition and regulatory team, discusses the recent Court of Appeal decision in *Unison Networks v The Commerce Commission*. Notwithstanding a unanimous finding that the Commission's initial price path threshold for large electricity lines companies was unlawful, the majority of the Court of Appeal went on to decline to set aside the thresholds on the basis that doing so would cause considerable disruption to the industry.

Electricity Commission issues green light on Transpower's new Auckland power line

The Electricity Commission has released its Notice of Intention to approve Transpower's amendment to the North Island Grid Upgrade Project that was submitted to the Electricity Commission as part of a Grid Upgrade Plan in September 2005. The public will be given an opportunity to make submissions after the release of the Commission's detailed statement of the reasons for its decision.

Utilities and resources

Telecommunications Amendment Bill makes its final assent

New Zealand is in line for significant changes in its telecommunication industry following the passage of the Telecommunications Amendment Bill late last year. In this commentary, Bell Gully senior solicitor David Blacktop provides a brief overview of some of the key provisions of the new legislation.

The Telecommunications Amendment Act was passed in December 2006 heralding the beginning of a new era in telecommunications regulation in New Zealand. The Act provides the legislative amendments necessary to implement the Government's decision to unbundle Telecom's local loop as well as providing a new "multilateral" benchmark agreement process for setting the terms and conditions for access to regulated telecommunications services. The Act also provides an accounting separation regime for Telecom to assist regulatory oversight.

Local loop unbundling

The local loop is the wire running from your house or business to Telecom's local exchange often referred to as the "last mile". The local loop is widely regarded as a natural monopoly because of the costs of duplicating a ubiquitous network in parallel to an existing network.

Local loop unbundling means that telecommunications providers will be able to obtain access to Telecom's last mile network. The Act provides the legislative framework for this to happen. Included in this is a description of the "local loop" service which Telecom must provide access to and a description of the method for determining costs – access seekers will have to pay a price reflecting total service long-run incremental cost, which is a cost-based pricing methodology.

Importantly, the final access agreements will be set between Telecom and access seekers under the Telecommunications Act. Another important amendment in the Act is the inclusion of a multilateral benchmark style service agreement process. This allows the Commerce Commission to undertake a process to set standard terms of access to allow an access seeker to obtain a regulated service without the need for an agreement with Telecom. This includes a standard price determination.

Accordingly, while the Act provides the framework for local loop unbundling to occur, until a standard terms agreement is in place, access seekers will not know the prices or terms on which they will be able to access the local loop. This might well determine whether local loop unbundling delivers the benefits the Government expects it to.

Accounting separation

While local loop unbundling was signalled in May this year, much of the interest and debate at the select committee level centred around decisions in relation to "splitting" Telecom's operating divisions. The rationale for these provisions being a desire to limit Telecom's ability to use its vertical integration to disadvantage other non-integrated providers.

When introduced, the Telecommunications Amendment Bill included a requirement for "accounting separation". Telecom will be required to disclose information about its retail and wholesale business activities as if those activities were operated as independent companies.

However, the Select Committee recommended that the Act also includes a requirement that Telecom establish and operate functionally separate business units for fixed network access services - which would essentially provide access to the local loop, other wholesale businesses, and its retail business.

Utilities and resources

A look back over oil and gas litigation in 2006

In this article Bell Gully senior associate [David Coull](#) reviews three recent cases involving New Zealand's oil and gas legislative regime each of which provide important lessons for lawyers and industry participants.

Since the re-determination of the Maui Field, the increase in the price of oil and gas has been matched by a proportionate increase in the level of oil and gas litigation. While it is fair to say that much of this litigation has related to disputes between Todd and Shell in relation to, among other things, pipeline access issues and the interpretation of their joint venture arrangements, the oil and gas legislative regime has also come under more scrutiny than ever before. Three cases decided in 2006 shed light on the operation of the Crown Minerals Act 1991 (Act) and the Minerals Programme for Petroleum (Minerals Programme) and indicate how the courts are likely to interpret the Act and the Minerals Programme.

Tap (NZ) Pty Ltd v Attorney-General

This case considered the rules relating to "priority in time" (PIT) applications for exploration permits. This method of application was introduced in the 2005 Minerals Programme to allow for competitive bids on a priority in time basis, by providing for a five working day period in which a subsequent application could be made following the initial application and then evaluating both applications in competition.

Tap filed a PIT application and Crown Minerals published details of the application on its website. Within the five working day period, Origin filed a PIT application in respect of the same area. Crown Minerals considered the applications on a competitive basis and awarded the permit to Origin. Tap sought judicial review of that decision but was unsuccessful in the High Court and the Court of Appeal.

The case turned on the interpretation of various provisions of the Minerals Programme. Three points in particular are noteworthy. First, both courts considered that the Minerals Programme's general intent is to encourage competitive bidding for permits. In that context, despite understanding Tap's grievance, the court interpreted the relevant provisions in light of the Minerals Programme's overall intent and held that Crown Minerals was entitled to treat the applications on a competitive basis.

Secondly, in light of the Tap decision, industry participants would be well advised to maintain a close watch on the Crown Minerals' website in respect of any acreage in which they may have an interest given the evidence presented by Crown Minerals that it has a policy of publishing details of PIT applications on its website.

Thirdly, the Court of Appeal commented that Tap should have applied for injunctive relief immediately upon discovering that Crown Minerals was going to consider Origin's application in competition with Tap's application. The Court of Appeal noted that Tap should not have awaited the outcome of that decision and in particular, should not have waited for Origin to incur significant expense before filing proceedings. Such an approach "essentially put the risk of the litigation on Origin's shoulders".

The Court of Appeal indicated that it would have denied discretionary relief in Tap's favour even if it had been successful in relation to the substantive legal issue. This is an important point in the context of an industry where decisions of third parties and regulators can lead to significant expenditure.

In light of the Tap decision, it now appears that prompt action by lawyers and industry participants is likely to be necessary in order to ensure that any judicial discretion does not weigh against granting the relief they may seek.

Bounty Oil & Gas NL v Attorney-General

Bounty held an exploration permit for offshore acreage in the Great South Basin. The permit's work programme required Bounty to, among other things, acquire certain seismic data. Bounty farmed out part of its permit interest to a third party (Electro) who then contracted with Fugro to perform the seismic work. Fugro obtained the data but Electro did not pay. Fugro subsequently terminated the contract (and sold the data to Exxon). Crown Minerals revoked the permit on the basis that Bounty had not complied with its permit obligations. Bounty applied for judicial review of the revocation.

The key issue was whether Bounty could excuse its failure to perform the work programme. Bounty pointed to Electro's default as a circumstance beyond its control and argued that third parties were

responsible for any default and the overall circumstances showed that Bounty had made a reasonable effort to ensure it complied with the work programme as it was required to do.

The court held that it was the permit holder's responsibility to ensure that any third party contractors (and any parties with whom those contractors had relationships) performed their contractual obligations so as to enable the permit holders to comply with their permit obligations. The court noted there was no evidence that Bounty could not itself pay Fugro nor any evidence of any serious efforts by Bounty to do so. The court emphasised that the contractual arrangements Bounty made for performing its obligation under the permit were entirely within its control. Electro's failure to pay Fugro was, therefore, irrelevant and the permit revocation was "fully justified".

The court also made an interesting observation as to who constitutes a "permit holder" for the purposes of the Act. The court commented that the term "permit holder" refers to the permit holders collectively (if there is more than one party with an interest in the permit) and not one of several permit holders individually. For example, the right of appeal against revocation belongs to "a permit holder". Notwithstanding that Bounty was not the only party which held an interest in the permit, the proceeding was brought by Bounty as sole plaintiff. However, given the lack of objection by the Crown, the court was happy to proceed on the basis that the appeal was brought by all permit holders (even though Bounty was the only person named as an applicant).

Greymouth Petroleum v Todd Taranaki Limited

This litigation concerned three main issues:

- Todd's right to use a deviated well crossing a permit boundary;
- rights to plug and abandon a suspended well; and
- rights to a lease for exploration and mining.

By way of background, PPL 38705 was issued in 1988 under the Petroleum Act 1937. It gradually reduced in size and passed through various hands and, in 2002, was transferred to Todd. Todd also held the adjacent Mangahewa mining permit. PPL 38705 expired in 2003 and Greymouth was subsequently issued a permit for that acreage.

The award of the vacant acreage to Greymouth awoke various dormant issues. In 2002, when the Mangahewa mining permit was carved out of PPL 38705, the Ohanga-2 well, an unsuccessful well drilled in 1998 to test the northern extent of the Mangahewa-2 discovery, was bisected by the permit boundary so as to leave its top portion and well head within Greymouth's permit and its bottom hole location within Todd's permit.

Greymouth argued, successfully, that Todd was not entitled to use Ohanga-2 (insofar as the well was within Greymouth's permit area) as such would involve exploration and mining in an area for which Todd did not have a permit. This was because the Act regulated both the location of exploration and mining activities and the location of minerals (and not just the latter) and also because the regulated activity occurred throughout the well bore and at the well head (and not just at the interface between the well and the reservoir).

In some senses, the judgment in Greymouth raises as many issues as it solves. It highlighted the need for agreement between adjacent permit holders in order for a well which crosses a permit boundary to be used for exploration or mining. Without the express authorisation of the servient permit holder, any exploration or mining in an area for which a person does not have the exclusive permit will amount to a breach of the Act. This would be the case even if the acreage was not subject to any minerals permit.

In respect of the abandonment of wells, the decision highlights Crown Minerals' policy of not including in exploration permits any well abandonment obligations (in contrast to their standard inclusion in mining permits). Explorers should be aware that it is currently the case that they may be under no obligation to plug and abandon a well unless an abandonment obligation is included in the work programme which forms part of the permit.

Conclusion

These cases are interesting for the lessons discussed above and also to note that the Crown continues to enjoy a discretion in relation to the regulation of the exploration and exploitation of its mineral estate. The Crown was successful in Bounty and in Tap and its evidence as to its interpretation of the Act played some

part in the outcome of the Greymouth case. This all serves to reinforce the importance for industry participants of a positive working relationship with Crown Minerals.

The Crown Minerals website referred to in this article is at: www.crownminerals.govt.nz

Utilities and resources

Draft New Zealand Energy Strategy released on 11 December 2006

The Energy Strategy, entitled "Powering our Future - Towards a sustainable low emissions energy system", sets out the Government's strategic vision for New Zealand's energy system until 2050. It is a relatively comprehensive document, and refers to several other related policy initiatives (including those relating to climate change and energy efficiency). This commentary outlines the Government's key objectives and proposals put forward for consideration in the Energy Strategy.

Identification of long term energy challenges

The introduction to the Energy Strategy seeks to set the scene by identifying the two major long term energy challenges facing New Zealand as the Government sees them. These are:

- responding to climate change and addressing carbon emissions from New Zealand's energy production and use; and
- delivering secure, clean energy to New Zealanders at affordable prices to support economic development, while being environmentally responsible.

The Energy Strategy is then broken into two main parts. The first part outlines the Government's broad policy objectives for New Zealand's energy future. The second part details the various initiatives the Government proposes to follow to achieve the identified goals.

Six broad areas of focus to improve the energy system

Part 1 of the Energy Strategy identifies six broad areas on which the Government intends to focus in order to improve New Zealand's energy system. In brief, these are:

- ensuring the Government provides strategic leadership and a clear direction in relation to the future of New Zealand's energy system;
- maintaining a secure energy supply – by ensuring supply is reliable and resilient;
- increasing the efficiency with which New Zealanders use energy - in order to reduce energy costs, enhance productivity and safeguard the environment;
- increasing the use of renewable energy resources (including new renewable energy sources such as wave and tidal electricity generation and the use of biofuels in the transport sector);
- reducing the level of New Zealand's greenhouse gas emissions; and
- promoting the use of environmentally sustainable technologies as soon as they become proven and economically viable.

Part 1 of the Energy Strategy also usefully identifies between five and ten initiatives or measures that are to be followed to achieve each of the broad objectives set out above. These are then described in the draft action plan (set out in Part 2 of the Energy Strategy) and the draft National Energy Efficiency and Conservation Strategy that also accompanies the Energy Strategy.

Some observations – climate change and security of supply

It is interesting to observe that although maintaining electricity supply in dry years and addressing the challenges posed by "peak oil" are clearly considered to be important policy objectives, the Energy Strategy states (page 19) "*the Government believes that the more serious and immediate challenge is climate change*".

Accordingly, a recurrent theme of the Energy Strategy is the Government's commitment to developing workable solutions to climate change concerns and implementing a strategy for the gradual reduction of New Zealand's greenhouse gas emissions. The Energy Strategy acknowledges that, in order to achieve

tangible results, targeted initiatives – on both a macro and micro level – will be necessary. It is perhaps not surprising the Energy Strategy has such a significant focus on climate change issues given the Government's various initiatives in recent years to address the potentially severe effects of climate change.

The Energy Strategy recognises that to effectively achieve the second key policy objective of having a secure energy supply all members of society – the Government, the energy producers and the energy consumers – must play an active role. The Government's stated goal is "reliability and resilience": the public must be able to reliably access energy services when required and those energy services must be able to cope with shocks and change – it appears that a "reliable" energy system will be a function of a "resilient" one. To achieve this, the Government advocates investment in core energy infrastructure such as grid and line arrangements in the electricity sector as well as the requirement to advance "energy diversity" – a catch phrase describing the use of different sources of supply.

Although the Energy Strategy promotes increased investment in renewable energy sources and associated technologies, the potential pitfalls of such sources of supply have not been ignored. In particular, security of supply issues exist in relation to the potential growth of the use of renewable sources of energy such as wind and hydro schemes. There is a concern that if New Zealand becomes overly reliant on wind and hydro power generation it may be susceptible to intermittent supply shortages. To address this concern, the Energy Strategy suggests a diversification of the location of wind farms but also that fossil fuel-based backup will continue to be required for some time to come. This makes even more acute the need to ensure that a secure gas supply is maintained given the limited future of the Maui gas field.

The Energy Strategy also recognises that the efficient use of energy has a central part to play in safeguarding New Zealand's security of supply, while also having ancillary environmental benefits such as reduced greenhouse gas emissions. It seeks to encourage both commercial and domestic consumers to use energy more efficiently. Achieving this goal in relation to domestic consumers is a clear challenge and the Government hopes to achieve this through widespread dissemination of information and the promotion of product labelling which clearly specifies the energy efficiency (or otherwise) of products. When used in conjunction with incentives and pricing mechanisms, the distribution of such information is seen as an effective means of encouraging consumers to use energy more efficiently.

The Energy Strategy concludes by stating that it will be necessary to consider what impact the choices made in relation to New Zealand's energy future will have on, in particular, energy security, greenhouse gas emissions and the affordability of New Zealand's energy. Clearly, the Government will be very interested in ascertaining whether industry participants feel that the many initiatives and policies detailed in the Energy Strategy have struck the "right" mix to ensure that these fundamental policy objectives are achieved over the long term.

Implications for the transport sector

The Energy Strategy specifically identifies the transport sector as a major consumer of energy and emphasises the importance to that sector of both security of supply and the gradual reduction of transport-related emissions. The Government advocates the introduction of biofuels and electricity as alternative sources of energy for the transport industry; although it is not debated that oil will remain an important source of transport energy for years to come. It is clearly hoped that the introduction of renewable energy sources such as biofuels will help the reduction of greenhouse gas emissions and ensure a steady stream of alternative energy to the transport sector.

In terms of actual initiatives, the Government proposes (among other things) a minimum biofuels sales obligation and the implementation of policies that promote the development of low emission vehicles such as hybrid plug-in and electric vehicles. Further initiatives include a restriction on the number of high emission vehicles that can be imported into New Zealand and the promotion of low carbon-related transport options by attempting to take more freight off the roads.

Submissions on the draft Energy Strategy

The Energy Strategy is a discussion paper and the Government has invited submissions on the proposals outlined – it is clear there is likely to be considerably more debate on New Zealand's future energy strategy in the coming months. Submissions on the Energy Strategy are due by **Friday 30 March 2007**.

This commentary is by Bell Gully senior associate [David Coull](#). David is based in our Wellington office and specialises in energy and corporate law.

To access a copy of the Energy Strategy visit the Ministry of Economic Development's website at www.med.govt.nz

Utilities and resources

Climate change and sustainable land management

At the end of 2006 the Government released a series of related discussion documents on the energy sector and climate change. These include a paper on the Government's proposed plan of action for the forestry and agricultural sectors with particular emphasis on the way forward for a carbon neutral economy and way of life.

The latest conclusions reached by the Intergovernmental Panel on Climate Change presented in Paris earlier this month have been seen as marking the day on which global thinking on climate change moved from debate to action. New science has allowed scientists making up the Panel to conclude that global warming was "unequivocal" and that human activity was "very likely" to blame.

In New Zealand the programme for action has already been put in place and, as indicated by the Prime Minister's 2007 Statement to Parliament, sustainability and climate change will continue to be a major focus over the coming years.

One of the most recent Government initiatives on climate change was the passage of the Climate Change Response Amendment Act in November last year. This legislation:

- made changes to the New Zealand Emission Unit Register to allow private New Zealand individuals and businesses to hold accounts with the Register and to trade in emission units (or, as they are more commonly known, "carbon credits"); and
- introduced the Permanent Forest Sinks Initiative which creates an opportunity for "Kyoto-compliant" landowners to gain financially through newly established permanent forest sinks. Landowners meeting the requirements of the initiative will be able to obtain tradable Kyoto Protocol compliant emission units in proportion to the carbon sequestered in their forests.

Following on from this legislation, in December 2006 the Government released a series of related discussion documents including:

- the Draft Energy Strategy (also discussed in this issue of *Commercial Quarterly*) along with two discussion papers,
 - Transitional Measures: Options to move towards low emission electricity and stationary energy supply and to facilitate a transition to greenhouse gas pricing in the future; and
 - Discussion paper on measures to Reduce Greenhouse Gas Emissions in New Zealand post-2012;
- the Draft New Zealand Energy Efficiency and Conservation Strategy; and the
- the Sustainable Land Management and Climate Change discussion document.

Submissions on these documents are due by 30 March 2007.

Sustainable land management and climate change

The Sustainable Land Management and Climate Change discussion document proposes policies for the agriculture and forestry sectors to be developed and implemented through a single, collaborative "Plan of Action". The Plan of Action is based on four pillars:

- adapting to climate change;
- reducing greenhouse emissions from land-based activities and creating carbon sinks;
- capitalising on business opportunities arising from climate change; and
- working together by creating linkages between the Plan of Action and other Government and industry led initiatives.

There are 16 possible options listed in Pillar Two, 10 in agriculture and six in forestry. The Government is looking for guidance on which to choose before deciding on a preferred policy package.

One of the more controversial proposals outlined in the paper is the Government's proposal to impose a flat deforestation charge on land use change from forestry to another use. The alternative option being proposed is to implement a tradable permit regime under which owners of forests would be required to hold a specified level of permits before they could switch to a different land use.

The discussion document also outlines measures to encourage afforestation through the provision of an "afforestation grant scheme" (AGS) or the choice between AGS and devolved Kyoto credits with associated liabilities.

The options put forward to address agricultural emissions include a tradable permits regime and offset schemes which would allow farmers to meet their agricultural emission liabilities by, for example, planting trees and producing biofuels.

To access a copy of the Sustainable Land Management and Climate Change discussion document visit the Ministry of Agriculture and Forestry's website at www.maf.govt.nz/climatechange

A Bell Gully newsletter discussing what trading "carbon credits" could mean to an individual or business in New Zealand will be available on Bell Gully's website soon.

For further information on climate change issues, please contact Bell Gully partner, [Simon Watt](#).

Utilities and resources

Electricity lines company fails in its attempt to get price thresholds set aside

David Blacktop, a senior solicitor in Bell Gully's Competition and Regulatory team, discusses the recent Court of Appeal decision in Unison Networks v The Commerce Commission. Notwithstanding a unanimous finding that the Commission's initial price path thresholds for large electricity lines companies was unlawful, the majority of the Court of Appeal went on to decline to set aside the thresholds on the basis that doing so would cause considerable disruption to the industry.

In a judgment¹⁴ issued on 19 December 2006, a majority of the Court of Appeal rejected Unison's claim to have the Commerce Commission's price path thresholds for large electricity lines businesses set aside.

Thresholds regime

The Commerce Commission is responsible under Part 4A of the Commerce Act for administering the regulatory regime applicable to large electricity lines businesses. This includes a requirement for the Commission to issue "thresholds for control" against which to judge the price and service performance of lines companies. If a lines company breaches the relevant thresholds, then the Commission must assess whether that company should be placed under price control.

Unison was the first company which the Commission identified as having breached the thresholds which the Commission preliminarily determined should be subject to price control. Subsequently, the Commission has reached similar preliminary decisions in relation to Vector and Transpower for control.

Unison's challenge

Unison challenged the thresholds used by the Commission to identify Unison as being a candidate for control – these thresholds included both:

- an initial price threshold, which required lines companies not to freeze prices; and
- a subsequent price threshold, which allowed companies to increase prices by an amount equal to $CPI - X$.

The court unanimously held that the purpose of the thresholds was "*to perform a screening or filtering function, which, over time, should capture those who are potential candidates for control.*" The candidates for control are those not acting in accordance with the purpose of the regime which provided that the purpose of the regime was to ensure lines businesses:

- (a) are limited in their ability to extract excessive profits; and
- (b) face strong incentives to improve efficiency and provide services at a quality that reflects consumer demands; and
- (c) share the benefits of efficiency gains with consumers, including through lower prices.

The court held that a "price freeze threshold" did not meet this purpose because "*an inefficient and high charging business could put itself out of reach of the potential for control simply by maintaining its monopoly pricing and low quality service.*" However, the court accepted that a CPI-X threshold did meet the statutory purpose because the thresholds did provide incentives to comply with (a)-(c) above.

Relief

The issue of relief was complicated by the fact that while the initial thresholds were unlawful, the subsequent revised thresholds were lawful. However, the revised thresholds took as their starting point

¹⁴ *Unison Networks Limited v The Commerce Commission* (Unreported decision, CA284/05, 19 December 2006)

the "unlawful" initial thresholds. This meant that setting aside the initial thresholds would bring down the revised and lawful thresholds.

The majority of the court declined to set aside the initial thresholds. While noting that "*there are strong cautions against exercising the discretion not to set aside an unlawful decision*", the majority accepted that setting aside the regime would "*cause considerable disruption to the industry and to the consumers.*" The minority Judge, O'Regan J put the threshold for declining to grant relief higher, describing the threshold as requiring "exceptional" circumstances. He was not satisfied that the disruption relief would cause to industry was "*so exceptional that relief should be withheld*".

Utilities and resources

Electricity Commission issues green light on Transpower's new Auckland power line

The Electricity Commission has released its Notice of Intention to approve Transpower's amendment to the North Island Grid Upgrade Project for the supply of electricity into, and north of, Auckland. Public consultation on Transpower's latest proposal will be held before the Commission makes its final decision.

On 31 January the Electricity Commission released its Notice of Intention to approve the revised Grid Upgrade Plan put forward by Transpower on 20 October 2006.

The latest Transpower proposal contains a suite of measures aimed at ensuring the security of electricity supply to Auckland, including the construction of a new transmission line between Whakamaru and Pakuranga which is capable of carrying 400kV but will only initially be energised at 220kV.

Background to the new proposal

In Transpower's original proposal submitted to the Commission in September 2005, Transpower proposed the construction of a new 400kV double circuit line between Whakamaru and Otahuhu. This construction was proposed as the first step in accomplishing Transpower's long-term strategic vision for 400kV to replace 220kV as the core grid transmission voltage. Transpower submitted that the proposal was necessary to avoid an increase in risk to security of supply in the Auckland and Northland region at times of peak loading from 2010.

However, on 27 April 2006, the Commission gave notice under rule 15.1 of Section III of Part F of the Electricity Governance Rules 2003 (Rules) that it intended to decline to approve the original proposal.

A full commentary on Transpower's original proposal and the Commission's reasons for declining the proposal is available in an earlier Bell Gully article on our website "[Electricity Commission turns down Transpower's proposed 400kV Whakamaru - Otahuhu line to be installed by 2010: A review](#)". In brief some of the key reasons given by the Commission for its refusal included:

- Transpower's analysis did not consider all alternative proposals and that its analysis of the benefits of its proposal were over-stated. In particular, Transpower's analysis did not consider the credible alternative project consisting of a new 220kV double circuit transmission line between Whakamaru and the South Auckland urban boundary (the alternative 220kV proposal);
- the Commission placed considerable value on delaying investment, giving time to consider advances in technology or changes in the electricity system that may mitigate against a new line being needed for Auckland, such as new generation in Auckland or Northland; and
- the Commission's estimate of the capital cost of Transpower's proposal was higher than Transpower's estimate.

On 31 May 2006, at Transpower's request, the Commission agreed to suspend its consideration of the original proposal. At this time, Transpower advised the Commission that it intended to provide another proposal for the Commission's consideration and that it no longer wished to progress the specific 400kV proposal to which the notice of intention issued on 27 April 2006 related.

On 20 October 2006, Transpower submitted its new proposal to the Commission.

The amended proposal

In brief, the amended proposal put forward by Transpower involves:

- building an overhead transmission line from Whakamaru to near the South Auckland urban boundary, which will be initially energised at 220kV, and later, when load growth requires it, modelled to be operated at 400kV following the construction of additional substations;

- a transition station near the South Auckland urban boundary where the overhead line will connect to underground cables;
- an underground cable section from the transition station to Pakuranga substation (rather than Otahuhu to increase diversity of supply);
- a second underground cable section to Otahuhu substation to be added at a future date; and
- the use of triples conductor to maximise the capacity of the overhead line.

The Commission's role

Transpower's proposal is an "investment proposal" which, if it is approved by the Commission, will allow Transpower to recover the approved costs of that investment from designated transmission customers in accordance with the transmission pricing methodology set out in Section IV of Part F of the Rules.

The Commission is required to consider and assess Transpower's proposal in accordance with the processes and considerations set out in Section III of Part F of the Rules. In particular, rule 13.4 provides that, in order to be able to approve the proposal, the Commission must be satisfied that the proposed investment:

- reflects good electricity industry practice in meeting grid reliability standards;
- complies with the processes set out in the Rules; and
- meets the requirements of the grid investment test. The grid investment test is set out in clause 4 of Schedule F4, and essentially requires that a proposed investment that is necessary to meet the reliability standard must maximise the expected net market benefit or minimise the expected net market cost compared with a number of alternative projects and that such conclusion is sufficiently robust having regard to the results of a sensitivity analysis (if one is conducted).

The Commission must also have in mind the objectives and outcomes specified in the latest Government Policy Statement (GPS) on Electricity Governance issued in October last year. These include:

- timely decision making;
- business confidence arising from more certainty around long-term planning and infrastructure development, adequate capacity to allow for the development of renewable generation; and
- priority to be given to reliability over cost where there is an element of uncertainty.

The Commission's decision

The Commission's decision to give preliminary approval of Transpower's Proposal was not unanimous but the Commission's Deputy Chair, Peter Harris, notes in his [Overview](#) of the decision that:

- all of the Commissioners agree that maintaining a reliable supply of electricity into and through Auckland requires a substantial upgrade of the transmission grid from South Waikato to Auckland;
- many of the elements of the upgrade are agreed, and are not considered controversial;
- substantial improvements in reliability and benefits have already been captured as a result of the review process that was undertaken since the original proposal was submitted as part of the Grid Upgrade Plan in September 2005.

At the time of publication the Commission had not released a detailed statement of its reasons for reaching the decision although it had indicated that this was to be available mid-February. Some of the reasons given for the decision outlined in the Overview include:

- the majority view that the proposal meets the requirement of the grid investment test with a result of similar magnitude to that described by Transpower in its application;

- the proposal is consistent with meeting its principal objectives under the Electricity Act 1992; and
- the proposal has a slight advantage to the alternative 220kV proposal in achieving the outcomes sought in the GPS.

However, it is to be noted that the Commission's approval is limited to the first stage of Transpower's plan. It does not include approval for the upgrading of the proposed transmission line to 400kV and this approval is not being sought by Transpower in its new proposal.

Next steps

After the Notice of Intention was released either a designated transmission customer, an authorised representative of parties substantially affected by the grid upgrade proposal, or Transpower, had the right to request the Commission to hold a public conference. The right to make this request closed on 15 February 2007.

The Commission has indicated on its website that it anticipates holding a public conference in late April or early May 2007. The public conference process includes the opportunity to make written submissions about the Commission's decision.

Following the public conference, the Commission may confirm or amend the Proposal. If no public conference is held, the Commission's decision, as set out in the Notice of Intention, is final.

For details on this decision visit the Electricity Commission's website at www.electricitycommission.govt.nz.

If you would like to know more about the decision or require assistance with the public consultation process, please contact any of our [electricity law team](#) or in the first instance please call:

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- [Commerce Commission](http://www.comcom.govt.nz) [www.comcom.govt.nz]
- [The Companies Office](http://www.companies.govt.nz) [www.companies.govt.nz]
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- [Takeovers Panel](http://www.takeovers.govt.nz) [www.takeovers.govt.nz]
- [NZ Stock Exchange](http://www.nzx.com) [www.nzx.com]

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