

22 March 2019

Miriam Dean QC
Chair
Expert Advisory Panel
Electricity Price Review
c/- Ministry of Business, Innovation & Employment
by email to energymarkets@mbie.govt.nz

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Dear Chair

Re: Electricity Price Review

Fonterra thanks the Expert Advisory panel for the opportunity to engage in this process through the MEUG session, participation in the cross-sector workshop and by providing feedback here.

Fonterra is a member of the Major Energy Users' Group (MEUG) and supports the points raised in that submission, as well as making the additional points in this submission.

Fonterra looks forward to further engagement with the expert advisory panel on this topic and is willing to discuss further any matters regarding this submission.

Yours sincerely

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D REINFORCING WHOLESALE MARKET COMPETITION		Fonterra comment
D1	Toughen rules on disclosing wholesale market information	<p>Fonterra agree with the EPR panel's summary of the current state, and the events of spring 2018.</p> <p>Without change, we do not have confidence that we will not see a repeat of the situation that arose in Spring 2018.</p> <p>We support the Electricity Authority's (EA) current work in this area.</p> <p>We agree with the panel comment that if the EA lacks sufficient power to enforce existing disclosure rules, it should be given.</p>
D2	Introduce mandatory market-making obligations	<p>Fonterra support the approach taken by the EPR panel.</p> <p>Fonterra supports mandatory market making. We would like to see companies in the market at all times, unless they can prove significant distress.</p> <p>It will be important to carefully consider and define the disclosure obligations to prove distress before companies can exit.</p>
D3	Make generator-retailers release information about the profitability of their retailing activities	<p>Fonterra favours this option, and would like to see more transparency and consistency of information.</p>
D4	Monitor contract prices and generation costs more closely	<p>Fonterra strongly supports this option.</p> <p>In an efficient market, prices should drive behaviour, but we aren't seeing this currently where bid price doesn't match bid scarcity.</p> <p>It is important that consumers have confidence in the electricity market, and that the spot market price is not showing excessive profits.</p> <p>We favour the move to real time pricing, and understand that this is already a priority work stream for the EA.</p> <p>We would like to see the EA monitoring each trading period looking for windfall profits.</p>
D5	Prohibit vertically integrated companies	<p>Fonterra do not support prohibition of vertically integrated companies, unless there is significant market failure. However, we believe there is an opportunity for more separation. It appears that vertically operated companies are currently protected from spot market pricing.</p> <p>We would like to see some tension added to market. This could be provided by a requirement for books to be out of sync. Generator/retailers could run two trading arms- wholesale and retail. (This is similar to how the milk price model operates in the dairy industry).</p> <p>There should be transparency around the wholesale transfer pricing between generation and retail in vertically integrated companies.</p>

E IMPROVING TRANSMISSION AND DISTRIBUTION		Fonterra comment
E1	Issue a government policy statement on transmission pricing	Fonterra would like to see the outcome of the transmission pricing methodology (TPM) before a Government policy statement is issued. We do recognise the panel's view that a government policy statement is an effective way for Government to express policy objectives, and understand from the workshop that the intention is to create a concise document that would not delay the TPM outcome.
E2	Issue a government policy statement on distribution pricing	Same feedback as E1
E3	Regulate distribution cost allocation principles	<p>Fonterra do not support this option.</p> <p>The allocation of distribution costs is different for residential vs business consumers. Industry connection is based on peak demand, whereas residential is based on a fixed load assumption per connection. Cost is higher relative to use for consumers so the cost should not be allocated on the same basis.</p> <p>Fonterra typically pays for the capital cost and ongoing maintenance cost of assets directly installed to supply our load. There is no cross-subsidisation from other consumers and often the infrastructure installed is solely for the end user.</p> <p>Recent CPP decisions have shown that the commerce commission does not have sufficient information on costs and asset condition during the DPPs resulting in the need for CPPs which trigger consumer price increases.</p>
E7	Strengthen the Commerce Commission's powers to regulate distributors' performance	Fonterra support further investigation
E9	Lower Transpower and distributors' asset values and rates of return	<p>This is an area that we would like to see further investigation. However, we do acknowledge the panels comment about terms of reference and technical complexity of this issue in the current review.</p> <p>Fonterra believes that WACC should be at the 50th percentile as the investment risk is low, and the risk from extreme events can be insured against.</p> <p>Fonterra notes that WACC is currently set at the 67% percentile and could lead to higher profits for EDBs. Fonterra also raises concerns that the potential for cross-subsidisation to occur between the regulated and non-core part of businesses, or via related party payments to reduce direct profits. These are both areas that could warrant further investigation.</p> <p>EDBs can put off R&M spending and then use CPP to fund asset improvement. We would like to see EDB asset management plans be lifted to the same quality as Transpower and cost benefit analysis done for all capital investment. This would reduce the risk of under maintaining assets and then driving capital spend increases in CPP requests thereby increasing the regulated asset base and hence profit.</p>