Fonterra Co-operative Group

June 2014

Submission to the Electricity Authority regarding the working paper: "Transmission pricing methodology review: Connection charges".

Fonterra Co-operative Group.

Overview

1. Fonterra Co-operative Group ("Fonterra") thanks the Electricity Authority ("EA") for the opportunity to make a submission in response to their working paper entitled "Transmission pricing methodology review: Connection Charges" ("Working Paper").

2. Fonterra is the world's largest global milk processor and exporter of dairy products and is at the heart of the New Zealand dairy industry, and the dairy industry is at the heart of the New Zealand economy. Through our integrated "grass to glass" supply chain we deliver high quality dairy ingredients and a portfolio of respected consumer brands to customers and consumers in over 140 countries around the world.

3. Fonterra is owned by approximately 10,600 farmer shareholders who supply Fonterra with greater than 17 billion litres of milk each year that is processed across 28 processing sites in New Zealand. All of these sites, and the farmers that supply the sites, are reliant on an efficient, reliable, and secure electricity transmission and distribution grid.

4. In the 2013 annual report, Fonterra recorded a net profit after tax of $736 million, on revenue of $18.6 billion, and a cash payout of $6.16 for the 2013 year for a 100 percent share-backed farmer – comprising a Farmgate Milk Price of $5.84 per kgMS and a dividend of 32 cents per share.

5. Fonterra is a member of the Major Electricity User Group ("MEUG") and in principle, supports the more detailed submission lodged by MEUG, except where a different view is expressed in this submission on the Working Paper.

6. The Working Paper is seeking feedback to assist the EA to decide on whether or not there are net benefits in:

   6.1. Addressing incentive problems resulting from the disparity between connection and interconnection charges;

   6.2. Moving from average replacement cost (ARC) based asset charges to depreciated replacement cost (DRC) based asset charges for connection pool assets;

   6.3. Moving closer to an actual cost-based methodology for the allocation of operating expenses within the connection pool.

7. This submission will provide feedback to the EA on the Working Paper.

General Feedback on the Working Paper

8. Fonterra submitted in March 2013 to the EA's October 2012 consultation paper "Transmission Pricing Methodology: issues and proposal" ("2012 TPM proposal"). Fonterra has reviewed the subsequent transmission pricing methodology ("TPM") working papers the EA has issued[1] and submitted on each via MEUG. Fonterra also lodged its own submission to the beneficiaries pays working paper.

9. As stated in our March 2013 submission to the EA's 2012 TPM proposal, "Fonterra views that the current TPM is working well, although acknowledge that it could be improved. Fonterra is generally supportive of the EA's review to explore how the TPM could be improved and encourages further exploration to ensure that if any improvement is implemented, that it is the correct solution and that it is implemented at the correct time."

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[1] Cost benefit analysis working paper, 3rd September 2013; Sunk costs working paper, 8th October 2013; Avoided cost of transmission working paper, 19th November 2013; Loss and constraint excess working paper, 21st January 2014; Beneficiaries pays working paper, 5th February 2014.

10. It does not appear that there is a problem to be addressed by this Working Paper. Many of the scenarios articulated in the Working Paper as a justification for a change (i.e. stranded assets, loop configurations) do not have examples of this occurring in practice as evidenced by Transpower's response to MEUG's questions. It is on this basis that we will, at this point in time, decline to comment on the other questions raised in the Working Paper.

11. Fonterra would like to note that it is difficult to comment on the DRC-based asset charge for connection assets proposal put forward in this Working Paper in isolation to the remainder of how the TPM will work. Fonterra also notes that is difficult to determine if the options put forward in this Working Paper are in the long-term benefit of consumers as a detailed qualitative and quantitative cost-benefit analysis ("CBA") has not been undertaken. Fonterra looks forward to reviewing a robust CBA as part of the second TPM issues paper.

12. In Fonterra's submission on the beneficiaries pays working paper, several positions that were put forward in our March 2013 submission on the 2012 TPM proposal were reiterated. In relation to this Working Paper, there are several additional views we would like to reiterate from our March 2013 submission:

    12.1. [Paragraph 39.2] If there is an increased number of submissions regarding Transpower's proposed investments, what is the likelihood that these will have any impact on the outcome of the Transpower investment decisions – will there be any changes to the Commerce Commissions process to accommodate for this?

    12.2. [Paragraph 40.1] Increased scrutiny on Transpower's proposed investments will not alter past investments...The level of proposed transmission investments that is planned for the future is minimal, compared to recent investments.

    12.3. [Paragraph 44] Any proposed change to the TPM should focus on the overall efficiency of the electricity industry for the long term benefit of electricity consumers and must not impose any short term disincentives on consumers. Increasing short term costs can put the viability of consumers at risk, especially energy intensive exporters.

13. Fonterra looks forward to commenting on the second TPM issues paper.

Please direct any queries regarding this submission to Fonterra's Energy Manager:	Linda.Mulvihill@fonterra.com