

22 September 2017

Commerce Commission
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PO Box 2351
Wellington
(Submitted via email to: powercocpp@comcom.govt.nz)

Fonterra Co-operative Group
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Attention: Matthew Lewer, Manager Price-Quality Regulation

Dear Matthew,

Re: PowerCo Customised Price Path Application

Fonterra thanks the Commerce Commission (CC) for the opportunity to provide feedback on the consultation, "Invitation to have your say on Powerco's proposal to change its prices and quality standards – Issues to explore and consider"¹ (*Issues Paper*).

Fonterra is a major electricity user and used approximately 1,100GWh of electricity last season (1 August 2015 to 31 July 2016, aka FY17). Fonterra's sites are located across New Zealand, resulting in Fonterra having relationships with 14 different electricity distribution businesses (*EDB*). Several of Fonterra's sites are within PowerCo's networks – including Pahiatua, Kapuni, Eltham, Kapiti – Palmerston North, Longburn, Whareroa, Tirau, Morrinsville, Waitoa, and Kapuni.

Fonterra is a member of the Major Electricity User Group (*MEUG*) and supports the points raised in that submission on this Issues Paper, except where they may differ by any points raised in this submission by Fonterra.

Fonterra provides feedback in the attached pages to this cover letter, based upon the Issues Paper grouping of issues into 7 topics.

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

Yours sincerely,

Linda Thompson
Sustainable Energy & Utilities Group Manager
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¹ <http://www.comcom.govt.nz/regulated-industries/electricity/cpp/cpp-proposals-and-decisions/powercocpp/powerco-customised-price-quality-path-proposal/>

1. Quality – issues relating to Powerco’s proposed quality measures & standards

- 1.1. The Issues Paper identifies that there are three key potential issues with Powerco’s proposal.
- 1.2. Fonterra agrees that Powerco’s proposed unplanned outage targets may not reflect the improvements to reliability that would be expected (and has been demonstrated) by Powerco’s increased expenditure. Fonterra supports the CC’s suggestion to adjust Powerco’s proposed quality targets to better directly reflect this expected improvement in network reliability.
- 1.3. Fonterra notes that Powerco’s CPP application appears to be based upon the recent increase in failure rate and that this trend has been forecast forward. Greater transparency on the mode of failure, root cause analysis of failures, and breakdown on the maintenance expenditure would assist with understanding if the increase in expenditure is warranted.
- 1.4. Fonterra agrees that Powerco’s proposal to exclude planned outages may weaken incentives for Powerco to minimise planned outages and their disruption to customers while undertaking the proposed CPP work program.
- 1.5. Fonterra also notes that communication of planned outages is very important. For example, advance notice of planned outages could allow dairy farmers to alter the time that they milk their herd on that day, allows Fonterra to vary scheduling times for milk collection off farms and deliver this milk to factories that are not impacted by a planned outage, and also allows Fonterra sites to prepare for planned outages. Without advance notice of planned outages, it can result in significant disruptions both on-farm and at the factory.
- 1.6. The frequency and duration of planned outages is also important, as this results in a disruption to operations both on-farm and at the factory.
- 1.7. Improved communication of outages via a range of different channels would also assist customers.
- 1.8. Powerco need to ensure that planned outages are minimised, both in the frequency and duration of outages, as well as being communicated in advance. The CC should consider how to capture this within a quality standard, rather than exclude this. For example, setting a maximum number of planned outages to a customer over a certain time period.
- 1.9. Powerco has suggested to provide increased reporting on a range of service measures, as well as progress against its planned CPP work programme, which are also important to ensure transparency on what is occurring. Fonterra supports these measures being provided and notes that there needs to be measurable goals with an appropriate incentive/penalty regime to ensure they are achieved.

2. Long term pricing impact of Powerco’s CPP proposal

- 2.1. The Issues Paper identifies that there is likely to be an increase in pricing post the CPP period. This is also supported by the analysis that NZIER had conducted for MEUG. It appears that the CPP is not for a “temporary catch up” on capital expenditure, but could become the norm for ongoing expenditure. The NZIER analysis also shows that there is a lack of improvement in the asset health index despite the increased expenditure which requires review by the CC.

- 2.2. The Issues Paper is not clear on what occurs if Powerco's expenditure is not as it has forecast – will this result in a reduction in MAR during or post the CPP period to account for this? It would be useful if the CC could provide some clarity on this point.
- 2.3. The Issues Paper does not appear to contain any analysis on Powerco's past expenditure and asset management program to assess if there should have been greater investment to avoid network degradation. This would be useful analysis for the CC to undertake to assess whether or not a CPP is warranted. MEUG's submission elaborates further on this point in the section regarding if Powerco has been constrained by the DPP price path.

3. Potential price volatility from WACC change during the CPP period

- 3.1. Fonterra does not support Powerco's suggested approach for varying the input methodology (IM) to forecast the DPP WACC for part of the CPP period, as there is uncertainty in what the future variables may actually be. Prices should be cost reflective as much as possible.

4. Asset health & criticality & its impact on capex forecasts

- 4.1. The Issues Paper notes that the verifier's review of Powerco's CPP application is that the asset health analysis may not be reasonable and may result in an overstatement of expenditure.
- 4.2. Powerco should prioritise expanding and embedding its asset criticality framework to ensure that it minimises the risk of over investment. This assessment must be undertaken alongside the asset health assessments to ensure that the correct investments are made and prioritised appropriately.
- 4.3. Fonterra would be willing to share its approach to asset management with the CC if that would assist with its review of Powerco's application.
- 4.4. Fonterra also suggests that the CC should appoint an independent expert who is a specialist in asset management to review the asset management plan and systems to ensure that the preventative maintenance and replacement plans are appropriate. This would assist with providing reassurance to customers that the proposed replacement and upgrade plans are actually warranted and also critique the approach to see if there is a more efficient way to achieve the desired outcome.

5. Network evolution capex

- 5.1. The Issues Paper notes that the verifier's review of Powerco's CPP application is that it doesn't have sufficient information to justify its proposed network evolution expenditure.
- 5.2. Providing a specific allowance for network evolution expenditure has the potential to set a precedent which is not appropriate.

- 5.3. It appears that there are numerous trials and investigations into similar technologies (e.g. battery storage, electric vehicle charging stations) across the numerous EDB's. There appears an opportunity for this to be more efficient and for knowledge to be shared across EDB's to avoid duplicated costs falling upon consumers across New Zealand.

6. Opex forecasts

- 6.1. The Issues Paper notes that Powerco's current investment rates led to a backlog of maintenance and vegetation work, but does not elaborate on why this has occurred in the past.
- 6.2. The Powerco CPP proposes to bring its fault calls in-house by establishing a call center. It would be good if an assessment of the benefits of this to consumers was articulated to assess if this is warranted.
- 6.3. The Issues Paper notes that the verifier identified that Powerco was not proposing any opex reduction initiatives. As Powerco can recover the full forecast opex from consumers during the CPP period, it would seem prudent that the forecast opex should be minimised to ensure that unnecessary costs are not incurred and passed onto customers. It is also uncertain what happens to consumer prices if the forecast opex is not spent, and how this underspend translates back into pricing. This pricing uncertainty also applies to capex underspend during the CPP period.

7. Deliverability risk of Powerco's CPP proposal

- 7.1. As outlined in the Issues Paper, there are risks associated with the delivery of the CPP work program. It is important that work is delivered to an appropriate standard and efficiently to ensure that costs are minimised.
- 7.2. The Issues Paper suggests that Powerco could provide high-level reporting against key milestones, as well as a detailed breakdown on a project basis, and Fonterra supports the provision of both.