

14th December 2017

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

Fonterra Co-operative Group
Private Bag 885, Cambridge, New Zealand
Victoria Road, Hautapu, Cambridge, New Zealand
www.fonterra.com

Attention: Dane Gunnell, Senior Analyst, Regulation Branch

Dear Dane,

Re: Powerco's proposal to Customise its Prices and Quality Path Standards Draft Decision

Fonterra thanks the Commerce Commission (CC) for the opportunity to provide feedback on the consultation, "Powerco's proposal to Customise its Prices and Quality Path Standards Draft Decision"¹ (*CPP Proposal*).

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 CPP Proposal, 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 Powerco's proposal to customise its prices and quality path standards draft decision grouping of issues into 5 decision areas.

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,

Tony Oosten
Manager Energy & Utilities Group
Tony.Oosten@Fonterra.com

¹ <http://www.comcom.govt.nz/regulated-industries/electricity/cpp/cpp-proposals-and-decisions/powercocpp/powerco-customised-price-quality-path-draft-decision/>

1. Draft decision on Powerco's capex forecasts

- 1.1. Fonterra supports the CC's decision to reduce Powerco's capex from \$873 million to \$825 million.
- 1.2. The rejection of the \$18 million for network evolution is supported as it means that a precedence for bringing the development of potentially new revenue streams into the CPP/DPP does not occur.
- 1.3. The implementation of a new ERP solution as funded in the ICT capex for value of \$23 million has not been identified in the decision as a potential risk for cost over runs and potential of negative impact on delivering Powerco's main capex projects if implementation issues occur.
- 1.4. As discussed in the MEUG submission, Fonterra still supports a rigorous cost benefit analysis to ensure the expenditure increase will deliver a measureable quality benefit to end users. If not included in this CPP, this discussion needs to be included in a post CPP decision review.

2. Draft decision on Powerco's opex forecasts

- 2.1. The draft decision paper does not propose any opex reduction initiatives.
- 2.2. The 7% increase in reactive maintenance as appose to a reduction over the CPP is a disappointment as it would be prudently expected that the significant increase in new equipment capex as well as a 33% increase in preventative and corrective maintenance would deliver at worst the same annual spend if not better performance. Failure mode analysis would assist in assuring that forecast expenditure will resolve the root cause of the failures and stop future repeat events. Fonterra recommends that the CC consider such analysis and for PowerCo to address the root cause of failures.
- 2.3. In paragraph 445 it is noted that reactive maintenance will reduce resulting in a cost reduction across future pricing periods, but our view is that those savings should be reflected in this CPP determination. Fonterra recommends that the CC consider reflecting these savings during this period of the price path.
- 2.4. In paragraph 420 it mentions Powerco's significant backlog of preventative and corrective maintenance issues but this is not reflected in the actual SADI and SAFI results. No detailed analysis of why this backlog occurred other than Powerco's spend limitation, and there is no discussion or quality metric to ensure this backlog does not occur again. Fonterra recommends that the CC consider how this issue is addressed.
- 2.5. The CC has indicated in this draft decision paper that there is no need for an independent review of Powerco's asset management plan even though the verifier has a concern about over forecasting of expenditure that then becomes part of the CPP. Fonterra shares this concern.

3. Draft decision on Powerco's price path

- 3.1. Fonterra still 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. Fonterra recommends that the CC does not adopt Powerco's approach to modify the IM.
- 3.2. Fonterra supports MEUG's submission that a comprehensive review of this CPP application has to occur to ensure that precedent setting has not occurred and the issue of having not signalled intentions to industry become the norm when faced with sound challenge to IM amendments.
- 3.3. The issue of under- and over-spend in the capex area is covered by the IRIS methodology, but the need for a revenue regulated industry to receive benefit from under spending is questionable. Risk levels are already built into the WACC. The previous DPP SADI and SAFI results do not reflect that there has been an underspend in capital and maintenance area's. The risk of capex over-spend should solely sit with Powerco and not the end customer as they have no control over the performance of Powerco to deliver projects on budget. That risk is already incorporated into the WACC and further compensation should not occur.
- 3.4. There is not an equivalent process like IRIS to adjust customer pricing if reduction in opex can be achieved from forecast amounts used to set the CPP. In paragraph 637 the CC clearly articulate this risk of under delivery but have chosen not to act on it just because of no previous signalling of this to industry. Fonterra's view is this CPP application negates the need to have previously signalled to industry.

4. Draft decision on Powerco's quality path

- 4.1. Fonterra acknowledges that the CC took on board the submissions around concern for increase network planned outages during this CPP period which for our shareholders could be worse than if the DPP was maintained due to no significant historic increase in SADI or SAFI. The inclusion of planned SADI and SAFI goes some way to ensuring end customer impact is minimised.
- 4.2. Fonterra still believes that there is a quality metric missing around planned outages that does not pick up the frequency of planned outages to the same end customers. For dairy farmers, multiple planned outages will be more inconvenient than a single planned outage. The frequency of planned outages on the same network quality metric will ensure Powerco plans their outages to ensure all necessary work is completed in the lowest number of outages on the same network.
- 4.3. For our dairy farmers and sites, there is still no quality measure that independently reviews the performance of Powerco and the retailers to ensure that they have reached all customers when communicating planned outages, as well as their performance in accurate and timely restoration time, and communication of the same during unplanned outages. Fonterra recommends that the CC consider the development and incorporation of such a quality metric to address these concerns.
- 4.4. Fonterra supports the CC's adjustment of the unplanned quality targets to reflect the expected improvements in network reliability that have driven the need for this CPP.

5. Draft decision to require Powerco to produce an annual delivery report

- 5.1. The APR document looks like a step in the right direction but there is no way to ensure customer feedback is taken on board to drive improvement in the following years. Fonterra recommends that CC consider how such an improvement could be incorporated.
- 5.2. Fonterra supports MEUG's submission around the questionable benefit of Powerco using staff time to generate a detailed report that has no contractually enforceable metrics. If the purpose of this report is purely for communication then can it be used for the post decision review to ensure that future CPP applications have a way outside of the quality targets to track customer feedback and responsiveness, as well as performance on delivery compared to the original CPP application.