



Dairy for life

1 August 2024

**'Reasons' paper in support of
Fonterra's Milk Price Manual for the
2024/25 Season**

1 August 2024

To: The Commerce Commission

1. Fonterra Co-operative Group Limited (Fonterra), certifies that:
 - a. in terms of section 150L(d) of the Dairy Industry Restructuring Act 2001 (the Act), Fonterra considers that its milk price manual to be applied in calculating Fonterra's Farmgate milk price for the 2024/25 financial year is, in all material respects, consistent with the purpose of subpart 5A of the Act; and
 - b. none of the circumstances set out in section 150G(1) of the Act have occurred with respect to the milk price manual to be applied in calculating Fonterra's Farmgate milk price for the 2024/25 financial year.
2. This certification is based on our interpretation of subpart 5A, and the other relevant assumptions, views and qualifications set out in the accompanying reasons provided pursuant to s 150L(e).

Signed by

Jackie Floyd
Director, Legal

Introduction

This paper provides the reasons in support of Fonterra's certification in respect of the Milk Price Manual to be applied in the calculation of Fonterra's Farmgate milk price in respect of Fonterra's 2024/25 Season (the F25 Manual), as required under section 150L of the Dairy Industry Restructuring Act 2001 (DIRA). The paper has been prepared under the oversight of the Milk Price Panel, and where relevant reflects the Panel's views.

Section 150L provides that Fonterra must:

- Provide the Commission with the milk price manual for the current season (i.e., the season commencing on 1 June 2024) (section 150L(a));
- Provide the Commission with any recommendations by the Milk Price Panel "in relation to the milk price manual" (section 150L(b));
- Notify the Commission of any change in the economic and business environment that, in Fonterra's view, requires a change to the milk price manual (section 150L(c));
- Certify to the Commission the extent to which Fonterra considers that the milk price manual is consistent with the purpose of subpart 5A of DIRA (section 150L(d)); and
- Provide the Commission with reasons for the view expressed in its certificate (section 150L(e)).

In addition, section 150G sets out the steps that Fonterra is required to take if it does not amend the Manual in accordance with a recommendation by the Panel, if it amends the Manual contrary to a recommendation by the Panel, or if it amends the Manual without having received a relevant recommendation from the Panel. We advise that none of these circumstances has occurred with respect to the F25 Manual.

On 19 June 2024 the board of Fonterra approved amendments to the Milk Price Manual, all of which were recommended by the Milk Price Panel. These amendments are set out in 'mark up' form in the Milk Price Manual attached to this paper. Where not obvious given their context, we explain their rationale below. In all other respects, the F25 Manual is identical to the F24 Manual, in respect of which Fonterra submitted a certification and reasons paper on 1 August 2023. Consistent with that paper, we have confined our comments in this paper to areas where our views have changed since previous reasons papers, or where we wish to provide additional information. In all other respects, we request that this paper be read in conjunction with our reasons papers submitted in respect of the 2012 – 2024 seasons.

We have also recently provided the Commission with our views on the appropriate interpretation of section 150A of DIRA in our 'reasons paper' in respect of the 2023/24 base milk price, and have not repeated these views in this paper.

This paper is intended to satisfy the section 150L(e) requirement to provide the Commission with the reasons for the view expressed in our certificate. The paper is organised as follows:

- In section 2, we set out, and explain the rationale for, the amendments to the Manual for F25.
- In section 3, we consider changes in the economic and business environment that are potentially of relevance to the calculation of the base milk price, and explain why we have not amended the Manual in response to these changes for the 2024/25 season.

The attachment to this paper comprises a 'marked up' version of the Milk Price Manual, identifying all amendments, and which satisfies the section 150L(a) requirement to provide the Commission with the manual for the current season.

We have separately provided to the Commission the recommendation by the Milk Price Panel in relation to amendments to the Milk Price Manual for F25, consistent with our obligation under section 150L(b).

Amendments to the Manual for F25

We have not made any changes to the Manual for F25 which will have any impact on the calculation methodology, the quantum of the base milk price, or the administration or governance of the base milk price calculation. Consequently, none of the amendments are inconsistent with the purpose of subpart 5A of DIRA.

The amendments principally fall into two categories:

1. Minor amendments to better align the explanations in Part A of the Manual of the operative rules contained in Parts B and C to the rules, and
2. Minor changes to language introduced in 2023/24 regarding the relevant provisions of the Dairy Industry Restructuring (Fonterra Capital Restructuring) Amendment Act 2022, as proposed by the Commerce Commission in its Final Report on the Manual for the 2023/24 season.¹

The amendments, other than self-explanatory changes, are explained in the table below.

Manual reference	Amendment	Comment
Part A, section 4.2, Farmgate Milk Price Commodity Business	The Farmgate Milk Price Commodity Business will sell its entire product on arm's length terms for delivery to shipment from the New Zealand wharf (i.e., on free alongside ship, or FAS, terms). (Similar amendments also made in two other instances in the same section and to Rule 4 in Part B. See the attached marked up Manual.)	A contextual amendment to better align the explanation in this section with the detailed rules in part B, which provide for the inclusion in the Milk Price revenue calculation of price-informing sales on a range of industry-standard terms, including cost-insurance-freight (CIF) as well as FAS terms.
Part A, section 4.3, Farmgate Milk Price Revenue	GlobalDairyTrade is owned by Fonterra, the European Energy Exchange (EEX) and New Zealand Exchange (NZX) in equal one-third shareholdings, and but is operationally and physically separate from Fonterra.	A tidy up amendment to reflect ownership of GDT.
Part A, section 4.4, Farmgate Milk Price Cash Costs	The other overhead costs of the Farmgate Milk Price Commodity Business, including site overheads, research and development costs, general overheads and corporate costs, will be established in every Review Period, based on an assessment of the budgeted costs of Fonterra in the Review Year, adjusted for the differences between budgeted costs and the costs Fonterra could reasonably be expected to incur if it only manufactured the Reference Commodity Products and undertook the activities performed by the Farmgate Milk Price Commodity Business . In intervening years, these costs will be increased by the annual movement in an appropriate index, such as the Producers Price Index or the Labour Cost Index to the extent they can reasonably be anticipated to be relatively constant across time . and will be checked for continued reasonableness by the Milk Price Group against movements in Fonterra's	A contextual amendment to better align the explanation in this section with amendments in recent years to the relevant operative rule, Rule 18 in Part B.

¹ [Final-report-Review-of-Fonterras-2023-24-Milk-Price-Manual-15-December-2023.pdf \(comcom.govt.nz\)](#)

	actual and budgeted costs, having particular regard to any significant change in Fonterra's overhead costs (such as any change resulting from a restructuring).	
Part A, section 4.4, Farmgate Milk Price Cash Costs	If there is reason to believe that the value of an input determined in a Review Year does not accurately reflect the actual value of that input that Fonterra would face if it manufactured the Reference Commodity Products using currently appropriate technology, and where the difference is material, the Milk Price Group will undertake a Within Period Review to determine an amended value.	A contextual amendment to align the explanation in this section with the operative rule, Rule 23 in Part B, which was amended in 2021.
Part A, Section 5.3, Milk Price Group	The day-to-day administration of the Manual will be carried out by an independent party operating at arm's length from Fonterra (the Milk Price Group) appointed by the Board in accordance with subsection 150EA(1) of DIRA, who will be responsible for calculating the Farmgate Milk Price and otherwise undertaking the functions and responsibilities assigned to the Milk Price Group under the Manual.	The Commission noted in paragraph 69 of the Final Report that these words should be added for completeness.
Part A, Section 6.1, Overview [of disclosure requirements]	The non-sensitive information (as defined in subsections 150JA(2) and 150QA(2) of DIRA) made publicly accessible by Fonterra in accordance with subsections 150JA(1) and 150QA(1) of DIRA.	The Commission noted in paragraph 71 of the Final Report that these section references to DIRA should be added to more fully reflect the disclosure requirements.
Part A, Section 6.4, Information Disclosure Relating to the Dairy Industry Restructuring Act	Except to the extent they contain information which Fonterra reasonably considers is commercially sensitive, subject to legal professional privilege, or personal information, Fonterra will make publicly available, modified where necessary to protect the disclosure of information that would be prejudicial to Fonterra's legitimate commercial interests, the Reports prepared for a Year by Fonterra under: <p>(a) Section 150L of the Dairy Industry Restructuring Act which, among other things, certifies to the Commerce Commission the extent to which Fonterra considers the Manual is consistent with the purpose of Subpart 5A of the Dairy Industry Restructuring Act 2001; and</p> <p>(b) Section 150T of the Dairy Industry Restructuring Act 2001 which, among other things, certifies to the Commerce Commission the extent to which Fonterra considers the assumptions adopted and the inputs and process used by Fonterra in calculating the Farmgate Milk Price for the relevant Season are consistent with</p>	The Commission noted in paragraphs 74 – 75 of its Final Report that Fonterra should better align this text with the new disclosure regime, by amending the introductory wording and by including a reference to the Commission's annual review of the Manual and s150JA of DIRA.

	<p>the purpose of Subpart 5A of the Dairy Industry Restructuring Act 2001.</p> <p>Fonterra will also make publicly available all information requested by or provided to the Commerce Commission in relation to the Commission's review of the base milk price for a Year (s150QA) and the Commission's review of this milk price manual (s150JA), other than information which Fonterra reasonably considers is commercially sensitive, subject to legal professional privilege, or personal information.</p>	
--	--	--

Changes in the Economic and Business Environment

We confirm we are not aware of any changes in the economic or business environment that would in our view necessitate a change to the Milk Price Manual for the F25 Season. In arriving at this view, we have had regard to the following:

- None of the amendments to the Milk Price Manual were prompted by changes in the economic or business environment.
- As a general matter, our view is that changes in the economic or business environment will in most circumstances not necessitate changes to the Manual, though they may result in changes in the approach taken to applying existing provisions of the Manual. Among other things, the existing provisions of the Manual could accommodate the changes in approach required to reflect the impact of changes in relative demand for (and profitability of) different product streams that affect industry-wide patterns of new investment, of assets becoming 'stranded' due to a significant reduction in milk supply, and one-off costs associated with natural disasters.