

16 November 2018



Matt Lewer
Manager-Regulation Development, Regulation Branch
Commerce Commission

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Dear Mr Lewer,

Submission on the Commerce Commission's Draft Report on the 2018/19 Milk Price Manual

Open Country Dairy (**Open Country**) is pleased to make this submission on the Commerce Commission's (**Commission**) draft report (**Draft Report**) on the 2018/19 milk price manual (**Manual**).

Specific changes

Fonterra's proposed changes to the language of the Manual are superficial, and do not meaningfully influence the substance of how the farmgate milk price is determined. On this basis we take the view that, in and of themselves, the changes do not impact on consistency with section 150A of Dairy Industry Restructuring Act one way or another.

That said, we question the value of these changes being made at all. Changes that do not move the Manual and the farmgate milk price closer to the statutory objectives of efficiency and contestability are an unnecessary distraction from genuine efforts to improve market outcomes.

Fonterra's 2018/19 Milk Price Manual leaves unaddressed fundamental concerns about the operation of the milk price monitoring regime. We set out key aspects of those concerns below, and implore the Commission to address Fonterra's lack of willingness to engage with these issues in its final report.

Ongoing transparency concerns

We are forced to reiterate our general concern that there is a lack of transparency within the Manual. This lack of transparency impacts negatively on market contestability in significant ways, meaning that it has real implications for any Commission decision regarding the consistency of the Manual with the section 150A purpose. Both the lack of transparency itself, and Fonterra's unwillingness to address previous recommendations made by the Commission to improve transparency, are serious concerns that remain unaddressed.

As we have previously noted to the Commission both formally and informally:

- A lack of adequate disclosure of Fonterra's processes and inputs in the Manual impedes the ability of the Commission to scrutinise the Manual (and consequentially the final milk price) properly. This impacts on the credibility of the Commission's draft view that the Manual is "largely consistent" with the section 150A purpose.

- A lack of transparency threatens market contestability because it puts Fonterra's competitors at a material disadvantage. Where Fonterra exercises an opaque discretion over processes and inputs, competitors are forced to second-guess Fonterra's approach to setting the milk price rather than simply being able to estimate a price benchmarked against market fundamentals.

Neither of these outcomes is consistent with the underlying purpose or the express provisions of DIRA. We implore the Commission to state this expressly in its final report.

The Commission has, in fact, already recognised that our concerns are genuine and valid. It has constantly reiterated to Fonterra that more transparency is desirable. Fonterra, however, has refused to act in accordance with the Commission's guidance. Last season we placed some emphasis on Fonterra's refusal to bring clarity to off-GDT sales, despite express assurances that this would occur. This season the Commission itself notes that farmer support, plant capacity and foreign exchange rates – all issues previously raised by independent processors – require greater clarity. It is now beyond time for the Commission to conclude that the Manual is in any way consistent with the section 150A purpose when the underlying transparency objectives of the milk price monitoring regime are manifestly not satisfied.

Stranding risk

This season, the Commission has specifically examined the treatment of stranding risk in the Manual.

Due to the truncated consultation timeframes that are a feature of the DIRA milk price monitoring regime, Open Country has not had sufficient opportunity to fully consider the implications of the Commission's draft conclusions. We reserve our position on the appropriateness of this draft conclusions for this and future seasons.

We do note that the discretion Fonterra retains under the Manual in respect of mothballing plant raises precisely the sorts of transparency issues that we have discussed above. It is reassuring that the Commission recognises this as an issue, but it must go further. The Manual is incomplete if it does not include clear, actionable principles and standards that observers can rely on to reasonably predict Fonterra's approach. In the absence of such principles and standards, the Commission is required to find that the Manual is not consistent with section 150A.

Concluding remarks

Open Country asks the Commission to think deeply about the in-market impacts of its determinations of consistency and respond proactively to the chronic lack of transparency in the Manual. The market needs the Commission to drive appropriate outcomes to expressly state that the Manual is inconsistent with the contestability standard where meaningful transparency is absent.

Thank you for the opportunity to comment on the Manual.

Best regards



Steve Koekemoer
Chief Executive Officer, Open Country Dairy Limited