

Departmental Disclosure Statement

Dairy Industry Restructuring Amendment Bill (No 3)

The departmental disclosure statement for a government Bill seeks to bring together in one place a range of information to support and enhance the Parliamentary and public scrutiny of that Bill.

It identifies:

- the general policy intent of the Bill and other background policy material;
- some of the key quality assurance products and processes used to develop and test the content of the Bill;
- the presence of certain significant powers or features in the Bill that might be of particular Parliamentary or public interest and warrant an explanation.

This disclosure statement was prepared by the Ministry for Primary Industries.

The Ministry for Primary Industries certifies that, to the best of its knowledge and understanding, the information provided is complete and accurate at the date of finalisation below.

23 July 2019

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Part One: General Policy Statement

Subparts 5 and 5A of Part 2 of the Dairy Industry Restructuring Act 2001 promote the efficient operation of dairy markets in New Zealand by regulating the activities of the dominant market player – Fonterra – to ensure New Zealand markets for dairy goods and services are contestable.

Fonterra's share of the market for farmers' milk has reduced from 96 percent in 2001 to around 80 percent in 2019. Despite its reduced market share Fonterra retains significant market power in terms of its national scale, large market share and incumbency advantage. It is therefore necessary to continue regulating the activities of Fonterra to promote the efficient operation of dairy markets in New Zealand.

However, changes to how Fonterra is regulated are needed to remove some regulatory requirements that are no longer necessary, to support and encourage better environmental performance of the dairy industry, to provide Fonterra with more flexibility to manage some aspects of its operations, and to provide increased clarity on aspects of the regulatory regime for both Fonterra and other dairy industry stakeholders. The Bill therefore provides for a package of measures to maintain regulatory disciplines on Fonterra's activities and enhance aspects of the dairy industry's performance as above.

This Bill amends Subparts 5 and 5A of Part 2 of the Dairy Industry Restructuring Act 2001 to –

- Allow Fonterra to decline applications from dairy farmers to become shareholders in, and supply milk to, Fonterra when it is unlikely that the applicant would comply with Fonterra's terms of supply. This is intended to support Fonterra's ability to manage aspects of farmers' on-farm performance more effectively and address reputational risks to Fonterra, and the dairy industry in general, which may arise from poor environmental, or other, on-farm performance.
- Clarify that Fonterra's terms of supply can include, and price differentiate on the basis of, for example, environmental, animal welfare, employment matters, and health and safety requirements. This will ensure that Fonterra is fully able to reward excellent on-farm performance of its farmer-shareholders as part of its business and strategic direction. Fonterra and its farmer-shareholders are expected to fully utilise the flexibility afforded by these amendments, including better management of discharges and greenhouse gas emissions.
- Provide Fonterra with discretion to refuse applications for applications to become shareholders in, and supply milk to, Fonterra if milk is supplied from newly converted dairy farms. This is to enable Fonterra to better manage uncertainty of future milk supply that may arise from dairy conversions, and the associated impacts on Fonterra's processing capacity and investment decisions.
- Allow Fonterra to issue capacity constraint notices for a period of up to three dairy seasons, rather than one, as now. This would provide Fonterra more flexible and realistic timeframes to plan and manage its future capacity investment.
- Limit Fonterra's discretion with regard to setting a key assumption (the asset beta) in its base milk price calculation. This is to reduce the risk of Fonterra using its discretion in a way that may impose higher than efficient costs on new and existing dairy processors, including Fonterra itself, while retaining the essence of

the existing light-handed milk price monitoring regime administered by the Commerce Commission.

- Require Fonterra to appoint one member of its Milk Price Panel on the nomination of the Minister of Agriculture. This is intended to further support the independence of Fonterra's Milk Price Panel.
- Require the Minister of Agriculture to carry out periodic time-bound reviews of whether the provisions of Subpart 5 and 5A of Part 2 of the Dairy Industry Restructuring Act 2001 should be retained, repealed or amended. This would provide regulatory certainty and a clear timeframe within which the dairy industry can plan and operate.

This Bill also amends the Dairy Industry Restructuring (Raw Milk) Regulations 2012 to –

- Reduce independent processors' eligibility to purchase up to 50 million litres of raw milk from Fonterra. Eligibility will cease once an independent processor has its own raw milk supply of 30 million litres or more in a single season (rather than three seasons now), sourced from dairy farmers or the wholesale raw milk market. This recognises that access to regulated milk from Fonterra is no longer essential to support investment in new large scale dairy processing facilities in New Zealand. At the same time, it maintains access to regulated milk for smaller processors that predominantly service the New Zealand domestic consumer market.
- Update the regulated terms on which Goodman Fielder – the only other large scale supplier of fresh milk to the New Zealand domestic consumer market – can purchase raw milk from Fonterra. This is to ensure that New Zealand consumers continue to have choice and access to basic dairy staples supplied by more than one processor at scale.

In addition, the Bill provides for a number of minor and technical changes to Subparts 5 and 5A of Part 2.

The Bill also amends Subpart 4 of the Dairy Industry Restructuring Act 2001 to reflect changes in responsibility for the management of the New Zealand Dairy Core Database (core database). Until 2014 Livestock Improvement Corporation (LIC) was responsible for managing the core database. That role is now carried out by DairyNZ, an industry good body, in accordance with the wish of the dairy industry. The Bill reflects the change in manager, and makes a number of consequential updates.

Part Two: Background Material and Policy Information

Published reviews or evaluations

2.1. Are there any publicly available inquiry, review or evaluation reports that have informed, or are relevant to, the policy to be given effect by this Bill?	YES
The Commerce Commission's report, titled: <i>Final report – Review of the state of competition in the New Zealand dairy industry – 1 March 2016</i> , is accessible at: https://comcom.govt.nz/_data/assets/pdf_file/0018/62370/Final-report-Review-of-the-state-of-competition-in-the-New-Zealand-Dairy-Industry-1-March-2016.pdf	

Relevant international treaties

2.2. Does this Bill seek to give effect to New Zealand action in relation to an international treaty?	NO

Regulatory impact analysis

2.3. Were any regulatory impact statements provided to inform the policy decisions that led to this Bill?	YES
<p><i>Regulatory Impact Assessments: Modifying Fonterra's obligations under the Dairy Industry Restructuring Act 2001 (DIRA) regulatory regime</i>, Ministry for Primary Industries, May 2019 (accessible at https://www.mpi.govt.nz/dmsdocument/34782-mo-redactions-for-public-release-regulatory-impact-assesments-watermarked-redacted)</p> <p>This document informed the policy decisions in relation to amendments to Subpart 5 and 5A of Subpart 2 of the DIRA and associated regulations. Some content has been withheld to protect information that would prejudice:</p> <ul style="list-style-type: none"> • the commercial position of the person who supplied or who is the subject of the information; and • the supply of similar information, or information from the same source, in the future. <p><i>Regulatory Impact Statement: Transfer of the Dairy Core Database and Herd Improvement Regulatory Review</i>, April 2014 (accessible at https://www.fisheries.govt.nz/dmsdocument/16810-transfer-of-the-dairy-core-database-and-herd-improvement-regulatory-review-regulatory-impact-statement/sitemap) This document informed the policy to enable the transfer of the dairy core database from Livestock Improvement Corporation to DairyNZ. Small amounts of content have been withheld:</p> <ul style="list-style-type: none"> • to protect information where the making available of the information would be likely unreasonably to prejudice the commercial position of the person who supplied or who is the subject of the information; and • maintain the effective conduct of public affairs through the free and frank expression of opinions by or between or to Ministers of the Crown or members of an organisation or officers and employees of any department or organisation in the course of their duty. <p><i>Requirements on Livestock Improvement Corporation and the role of the Access Panel; Regulatory Impact Statement</i>, Ministry for Primary Industries, July 2014 (accessible at https://www.mpi.govt.nz/dmsdocument/3917-requirements-on-livestock-improvement-corporation-and-the-role-of-the-access-panel-regulatory-impact-statement/sitemap)</p> <p>This document informed the policy to amend Subpart 4 of the DIRA. Small amounts of content have been withheld:</p> <ul style="list-style-type: none"> • to protect information where the making available of the information would be likely unreasonably to prejudice the commercial position of the person who supplied or who is the subject of the information; and • maintain the effective conduct of public affairs through the free and frank expression of opinions by or between or to Ministers of the Crown or members of an organisation or officers and employees of any department or organisation in the course of their duty. 	
2.3.1. If so, did the RIA Team in the Treasury provide an independent opinion on the quality of any of these regulatory impact statements?	YES

On 10 May 2019, The Treasury provided the following opinion on the Regulatory Impact Assessments relating to changes to Subpart 5 and 5A of Subpart 2 of the DIRA and associated regulations:

RIA 1 – Obligation to Accept all Milk from New and Existing Farmer-Shareholders

The panel considers that the RIA on the 'Obligation to Accept all Milk from New and Existing Farmer-Shareholders' meets the quality assurance criteria. While technically complex, a strong case has been made to refuse applications from farmers if their milk supply is unlikely to comply with Fonterra's terms of supply. The case is not as strong for refusing applications from newly converted dairy farmers because although they have more choice than existing dairy farmers who they sell to, their choices are still limited. The RIA indicates that these proposals balance reducing costs and the unintended consequences of the open entry requirements for Fonterra, while ensuring minimal impact on the overall effectiveness of the regulatory discipline on Fonterra. Careful drafting of the legislative provisions will be required to minimise the risk of gaming by Fonterra.

RIA 2 - Obligation to Calculate a Benchmark Milk Price

While presented in a complex manner, the panel considers that the RIA on the 'Obligation to Calculate a Benchmark Milk Price' meets the quality assurance criteria. There are risks and costs associated with the proposed amendment to Fonterra's benchmark price calculation, but they are likely to be small relative to the benefits. This view is supported by the Commerce Commission's extensive consideration of the issue.

RIA 3 – Obligation to Sell up to 50 million litres of Raw Milk to Independent Processors

The panel considers that the RIA on the 'Obligation to Sell up to 50 million litres of Raw Milk to Independent Processors' meets the quality assurance criteria. The proposed change is essentially addressing a regulatory stewardship issue by removing regulation relating to the eligibility criteria for access to regulated milk from Fonterra that is no longer needed. The proposed regulatory change is based on evidence of past industry practice, focussing mainly on existing processors and it is less clear what this means for new dairy processors.

RIA 4 – Obligation to Sell up to 250 litres of Raw Milk to Goodman Fielder

The panel considers that the RIA on the 'Obligation to Sell up to 250 litres of Raw Milk to Goodman Fielder' meets the quality assurance criteria. It is an overly complex presentation of what is essentially a regulatory stewardship issue arising because the regulated terms on which Goodman Fielder can access raw milk from Fonterra are no longer current.

RIA 5 – DIRA Review and Expiry Provisions

The panel considers that the RIA on the 'DIRA Review and Expiry Provisions' meets the quality assurance criteria. The problem definition is clear and a range of options around expiry and review provisions has been outlined. A sound case has been made for regular reviews by MPI to balance the risk of Fonterra being regulated for longer than necessary and the risk of regulation being removed too early. A six yearly review cycle would help to balance the regulatory outcomes sought and the cost of the reviews, with out-of-cycle reviews if required.

The Treasury did not assess the regulatory impact statements relating to changes to subpart 4 of the DIRA. Independent quality assurance was undertaken by the Ministry for Primary Industries.

2.3.2. Are there aspects of the policy to be given effect by this Bill that were not addressed by, or that now vary materially from, the policy options analysed in these regulatory impact statements?

YES

The proposed amendment to require Fonterra to appoint one member of its Milk Price Panel on the nomination of the Minister of Agriculture was not addressed by the policy options analysed in the Regulatory Impact Assessments.

This policy was identified and agreed to in the course of Cabinet’s deliberations on other policy recommendations covered by the Regulatory Impact Assessments.

Extent of impact analysis available

2.4. Has further impact analysis become available for any aspects of the policy to be given effect by this Bill?	NO

2.5. For the policy to be given effect by this Bill, is there analysis available on:	
(a) the size of the potential costs and benefits?	YES
(b) the potential for any group of persons to suffer a substantial unavoidable loss of income or wealth?	YES
Information on these matters is outlined in: <ul style="list-style-type: none"> • <i>Regulatory Impact Assessments: Modifying Fonterra’s obligations under the Dairy Industry Restructuring Act 2001 (DIRA) regulatory regime</i>, Ministry for Primary Industries, May 2019 (accessible at https://www.mpi.govt.nz/dmsdocument/34782-mo-redactions-for-public-release-regulatory-impact-assesments-watermarked-redacted) • <i>Regulatory Impact Statement: Transfer of the Dairy Core Database and Herd Improvement Regulatory Review</i>, April 2014 (accessible at https://www.mpi.govt.nz/law-and-policy/legal-overviews/regulatory-impact-statements/). 	

2.6. For the policy to be given effect by this Bill, are the potential costs or benefits likely to be impacted by:	
(a) the level of effective compliance or non-compliance with applicable obligations or standards?	YES
(b) the nature and level of regulator effort put into encouraging or securing compliance?	YES
Information on these matters is outlined in: <ul style="list-style-type: none"> • <i>Regulatory Impact Assessments: Modifying Fonterra’s obligations under the Dairy Industry Restructuring Act 2001 (DIRA) regulatory regime</i>, Ministry for Primary Industries, May 2019 (accessible at https://www.mpi.govt.nz/dmsdocument/34782-mo-redactions-for-public-release-regulatory-impact-assesments-watermarked-redacted) 	

Part Three: Testing of Legislative Content

Consistency with New Zealand's international obligations

3.1. What steps have been taken to determine whether the policy to be given effect by this Bill is consistent with New Zealand's international obligations?

Consultation with the Ministry of Foreign Affairs and Trade.

Consistency with the government's Treaty of Waitangi obligations

3.2. What steps have been taken to determine whether the policy to be given effect by this Bill is consistent with the principles of the Treaty of Waitangi?

Consultation with Te Puni Kōkiri and Te Arawhiti.

Consistency with the New Zealand Bill of Rights Act 1990

3.3. Has advice been provided to the Attorney-General on whether any provisions of this Bill appear to limit any of the rights and freedoms affirmed in the New Zealand Bill of Rights Act 1990?

YES

Advice provided to the Attorney-General by the Ministry of Justice, or a section 7 report of the Attorney-General, is generally expected to be available on the Ministry of Justice's website upon introduction of a Bill. Such advice, or reports, will be accessible on the Ministry's website at <http://www.justice.govt.nz/justice-sector-policy/constitutional-issues-and-human-rights/bill-of-rights-compliance-reports/>.

Offences, penalties and court jurisdictions

3.4. Does this Bill create, amend, or remove:

(a) offences or penalties (including infringement offences or penalties and civil pecuniary penalty regimes)?

YES

(b) the jurisdiction of a court or tribunal (including rights to judicial review or rights of appeal)?

NO

The Bill applies the existing offence in section 150E(3) to a new provision that would require Fonterra to appoint one member of its Milk Price Panel on the nomination of the Minister of Agriculture.

The Bill provides for the existing offences and penalties that currently apply to Livestock Improvement Corporation Limited, as the manager of the New Zealand Dairy Core Database, to now apply to any other party appointed as the manager of the New Zealand Dairy Core Database.

3.4.1. Was the Ministry of Justice consulted about these provisions?

YES

The Ministry of Justice was consulted on these provisions and did not raise any issues.

Privacy issues

3.5. Does this Bill create, amend or remove any provisions relating to the collection, storage, access to, correction of, use or disclosure of personal information?

NO

External consultation

3.6. Has there been any external consultation on the policy to be given effect by this Bill, or on a draft of this Bill?	YES
<p>Following the release of the terms of reference for the DIRA review, MPI undertook pre-engagement with key stakeholders and commissioned independent economic analysis to identify issues and possible options for change. This informed the development of a public discussion document, <i>Review of the DIRA and its Impact on the Dairy Industry</i>, which was released in November 2018 and is accessible at: https://www.mpi.govt.nz/dmsdocument/31410-review-of-the-dairy-industry-restructuring-act-2001-discussion-document</p> <p>Following the public release of the discussion document, MPI undertook an extensive public consultation process including 13 public meetings, and 22 one-to-one meetings, with dairy processors and other key stakeholders, such as farmer representatives, Māori landowners and environmental NGOs. To better inform these meetings, MPI published all material derived from its preliminary analysis, including the findings of the independent economic analysis, preliminary input and commentary provided by Fonterra and other dairy processors, and provided an online questionnaire for interested persons who did not wish to write their own formal submission.</p> <p>MPI received 188 written submissions on the discussion document. These submissions expressed a range of views, from those who believed competition was sufficient and that the DIRA provisions should be repealed to those that advocated retaining and/or strengthening of the existing DIRA requirements. Further detail of the consultation process and a summary of key themes arising from stakeholder meetings and submissions is included in Appendix Three of the Cabinet paper, accessible at: https://www.mpi.govt.nz/dmsdocument/34779-mo-redactions-dira-cab-paper-watermarked-redacted</p> <p>DairyNZ consulted on a proposal to transfer the New Zealand Dairy Core Database from LIC to DairyNZ in 2010, following a recommendation by the Anderson Committee in 2009. MPI consulted on this in 2011 and formally issued a discussion document covering the regulatory regime for the dairy core database in 2012. LIC consulted with its farmer shareholders in 2012, who voted in support of the transfer.</p>	

Other testing of proposals

3.7. Have the policy details to be given effect by this Bill been otherwise tested or assessed in any way to ensure the Bill's provisions are workable and complete?	NO

Part Four: Significant Legislative Features

Compulsory acquisition of private property

4.1. Does this Bill contain any provisions that could result in the compulsory acquisition of private property?	NO

Charges in the nature of a tax

4.2. Does this Bill create or amend a power to impose a fee, levy or charge in the nature of a tax?	YES
The Bill amends the regulation-making power to levy Fonterra for the costs of the Commerce Commission to administer the DIRA. The power to make levy regulations already existed in section 134 of the DIRA, and is being amended to streamline the process for making regulations. The general scope of the power remains the same, and the standard requirements and process for making regulations would apply.	

Retrospective effect

4.3. Does this Bill affect rights, freedoms, or impose obligations, retrospectively?	NO

Strict liability or reversal of the usual burden of proof for offences

4.4. Does this Bill:	
(a) create or amend a strict or absolute liability offence?	NO
(b) reverse or modify the usual burden of proof for an offence or a civil pecuniary penalty proceeding?	NO

Civil or criminal immunity

4.5. Does this Bill create or amend a civil or criminal immunity for any person?	NO

Significant decision-making powers

4.6. Does this Bill create or amend a decision-making power to make a determination about a person’s rights, obligations, or interests protected or recognised by law, and that could have a significant impact on those rights, obligations, or interests?	YES
<p>The Bill establishes two additional exceptions to the requirement for Fonterra to accept applications from dairy farmers to become shareholders (and supply milk to) Fonterra. The new exceptions relate to dairy farmers who are unlikely to comply with Fonterra’s terms of supply and/or those who are converting their productive land to dairy. While Fonterra would no longer be required to accept shareholder-suppliers, under the proposed exceptions, it may nevertheless choose to do so. Fonterra’s decisions on whether or not to accept supply, under the proposed amendments, would be based on a case-by-case basis and would inherently involve the exercise of discretion.</p> <p>The Bill establishes safeguards around this new discretion by setting specific criteria for when it may be applied, and a clear process for Fonterra to seek further information if required. The new exceptions will also be subject to the existing dispute resolution provisions that enable a farmer to seek a determination from the Commerce Commission.</p>	

Powers to make delegated legislation

4.7. Does this Bill create or amend a power to make delegated legislation that could amend an Act, define the meaning of a term in an Act, or grant an exemption from an Act or delegated legislation?	NO

4.8. Does this Bill create or amend any other powers to make delegated legislation?	YES
<p>The Bill includes a new regulation-making power and makes regulations to require the provision of information from Fonterra and independent processors to enable MPI to monitor the developments in the wholesale (e.g., processor to processor trades) milk market. This mirrors an existing power to require the provision of information to monitor the farm gate (farmers to processors trades) milk market.</p> <p>The Bill also includes a new regulation-making power to enable regulations to specify types of conclusive evidence for applicants to supply to Fonterra to demonstrate that their farm is not a new dairy conversion. The ability to specify conclusive evidence could provide Fonterra and farmers with greater clarity, and make the application and determination process more straightforward.</p> <p>In addition, the Bill amends an existing regulation-making power that provides for a levy to be imposed on Fonterra to recover the costs incurred by the Commerce Commission in administering the DIRA. The amendments would allow for the current levy regulation-making process to be simplified, while retaining the existing requirement for the Minister to consult with Fonterra and the Commerce Commission before making these regulations.</p> <p>The standard process for the development and approval of regulations will apply to all new regulation-making powers.</p> <p>The Bill includes an expansion of existing regulation-making powers at clauses 15-17 to provide for the confidentiality and maintenance of the dairy core database. It extends current regulation-making powers, which are able to be applied to LIC, to any previous, current and intended managers of the dairy core database.</p>	

Any other unusual provisions or features

4.9. Does this Bill contain any provisions (other than those noted above) that are unusual or call for special comment?	NO