



FURTHER CONSULTATION: FIBRE INPUT METHODOLOGIES DETERMINATION
2020

Submission to the Commerce Commission

PUBLIC VERSION

13 August 2020

INTRODUCTION

1. Vocus welcomes the opportunity to submit in response to the “[Further consultation] Fibre Input Methodologies Determination 2020” and “Fibre Input Methodologies: Further consultation draft - reasons paper”, 23 July 2020.
2. We acknowledge the challenges the Commission is having in developing and implementing the Input Methodologies (IMs), and new Part 6 fibre price-quality regulation (PQR), in a very constrained time period. The constraints are evident in some of the trade-offs and pragmatic judgements the Commission appears to be making, such as the timeframes and processes for Chorus’ base capex and connection capex baseline proposal submission date.
3. If you would like any further information or have any queries about this submission, please contact:

Quentin Reade
Head of Communications
Vocus Group (NZ)
Quentin.Reade@vocusgroup.co.nz

OVERVIEW COMMENTS

4. A key concern for Vocus is that the need to develop the IMs, and make the first PQR determination, within a tight and challenging time-frame does not undermine the integrity of the new Part 6 fibre regulation.
5. Elements of the regime such as Independent Verification, and audit and certification requirements for capex proposals, are extremely important for determining the extent to which Chorus’ proposals and data can be relied on or used as an input into the PQR determinations. We would not support weakening of the proposed requirements such as removal of audit requirements that information is true and correct.
6. Another key element, which remains unresolved, is how the Commission will determine the value of the ‘financial loss asset’. The approach the Commission has proposed risks providing Chorus with a substantial windfall gain (locking in excess returns into the assets value) to the direct detriment of consumers. The material nature of this element may warrant the type and level of analysis the Commission conducted in its Part 4 WACC percentile review in 2014 to determine the best approach.
7. The distinction the Commission will need to make between Chorus’ PQR and Information-Disclosure (ID)-only fibre assets adds a layer of complexity to the cost allocation rules. We support the use of an accounting-based allocation approach (ABAA) as proposed by the Commission (and not the optional variation accounting based allocation approach (OVABAA)). Care will be needed to ensure no element of the ID-only fibre business’ costs or losses get incorporated into the PQR fibre business or ‘financial loss asset’.

OUR COMMENTS ON THE DRAFT REASONS PAPER AND DETERMINATION

8. We have the following specific comments on the consultation:
- (i) **Services included in the regulated fibre service:** We welcome the Commission's further confirmation of the scope of the regulated fibre service. It is appropriate that the Commission has *"not exclude[d] the possibility that other services might be included within FFLAS over time"*.
 - (ii) **Crown financing benefit:** We do not consider the Commission's judgement about the financing rate or adoption of a 25 basis points discount has been well established. It isn't clear the proposed approach is needed to *"minimise the risk of ... incentivising Chorus to retire Crown financing early"*. Consistent with debt:equity ratio settings in the WACC method, the Commission could set financing costs independently of how Chorus' actually finances its debt e.g. the option in paragraph 3.48.3. This would result in lower prices for consumers. It is unclear how such an approach would *"override"* or *"undermine the contract between the Crown and Chorus"*. It is also unclear what the relevance is of the fact the contract *"allows for early repayment of equity securities"*.
 - (iii) **Capital contributions:** We welcome that the Commission *"agree[s] with Spark that the funding of non-standard connections should be treated as a capital contribution"*.
 - (iv) **Financial loss asset:** We welcome the Commission's further confirmation that *"the ability to recover revenue from the financial loss asset is closely linked to the ability to recover revenue from the "main RAB"*, *"This means that, as the size of the RAB decreases due to removing deregulated cost components, so too does the ability to recover revenue from the financial loss asset"* and *"the value of the financial loss asset that will be removed from the RAB following deregulation decision is linked to the value of the UFB assets in the RAB at the time of implementation"*.
 - (v) **Granularity of asset data:** We query the commentary from LFCs about granularity of asset data. It would be surprising if the level of granularity they are able to provide is driven solely from GAAP requirements and not good practice asset management. We agree with the Commission that regulators/providers should be expected to *"have kept[/keep] additional records to maintain the minimum level of additional information that is aligned with good telecommunications industry practice"* and *"The information captured under GAAP is not necessarily sufficient to efficiently manage a telecommunications network"*. If the LFCs have a different perspective it will be important to understand why.
 - (vi) **Cost allocation:** The use of ABAA (and not OVABAA) for cost allocation between the PQR and ID-only fibre businesses is appropriate. Care will be needed to ensure no element of the ID-only fibre business' costs or losses get incorporated

into the 'financial loss asset'. We agree that it would not be possible to “*carry out cost allocation between different classes of regulated FFLAS using the existing cost allocation methodology*” for the reasons the Commission has provided.

- (vii) **Geographic disaggregation:** Chorus should be required to breakdown costs and assets by UFB area.
- (viii) **Capex IM:** We note and welcome that the Commission has made enhancements to the Chorus' Capex IM.
- (ix) **Audit and certification:** Audit and certification requirements for capex proposals will be extremely important for ensuring Chorus' proposals can be relied on or used as an input into the PQR determinations. We would not support any further weakening of the proposed requirements e.g. we continue to support that the audit requirements include that the information is true and correct.
- (x) We agree that external audit of base capex should be mandatory. We note and welcome that Transpower has sought external audit on a voluntary basis for its last two proposals.
- (xi) **Re-openers:** We agree that “*loss of supply ... caused by the regulated provider's action or neglect*” and “*a situation that the regulated provider could have prevented or overcome*” should not qualify for a reopener.
- (xii) We support the changes made to clause 3.9.6 in relation to error reopening.
- (xiii) **Quality IM and quality determination:** We note the Commission's commentary on the level of detail in the Quality IM versus the PQR quality determination. The submissions we have made, including the joint 2degrees, Spark, Vocus and Vodafone submission, will be relevant considerations for the draft PQR determination.
- (xiv) **Alignment with Part 4 reviews:** We agree with the Commission's intention to align cost of capital IM reviews across Part 4 Commerce Act and Part 6 Telecommunications. The cost of capital IM is the most obvious example where this may be desirable, given the heavy overlap (non-industry specific matters), but we are opening to the Commission identifying and considering other common areas jointly on a case-by-case basis. For example, the issues around what is included and not included as pass-through and recoverable costs has direct cross-over with Part 4 Commerce Act, reflected in the various submissions from ENA et al on this topic.
- (xv) **COVID-19 and WACC:** We agree with the Commission position not to alter WACC in response to COVID-19. Any decision to the contrary would have potential implications for Part 4 regulation.