



Fibre ID and PQ draft decisions

Cross-submission | Commerce Commission

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Executive Summary

Thank you for the opportunity to provide feedback on the submissions made on the draft Amendments to Fibre Input Methodologies decision (**the draft**).

Chorus generally supports the Commission's proposed amendments and proposes wide ranging amendments to the treatment of Crown Financing, the wash-up, capex and various assets, and to recalculate the stranding allowance prior to December 2021.

Chorus' additional proposals are all substantive changes to how the price quality path will be determined, yet none of them are consistent with the scope of the s179 notification to amend the IMs to enable the anticipated transitional and actual initial RAB process and to implement specific planned draft decisions.

Accordingly, the Commission cannot consider Chorus' additional proposals as part of this process. If the Commission did decide to consider Chorus' proposed amendments, it should set out the scope of the considerations and process as required by s179 of the Act.

In any case, we do not believe that the Commission should consider further amendments prior to making final decisions later this year. Chorus' proposals relating to Crown Financing, the stranding allowance and washup all traverse ground that was considered at length through the IM process, and we are still only part way through the process of implementing those decisions. We are not aware of any underlying change in the market from when the IMs were completed in October 2020 that suggests a rethink of the stranding allowance. Customers continue to migrate off poorly performing legacy copper services on to wireless and fibre alternatives, wireless provides an option for customers who previously had no broadband service, and we continue to see strong growth in UFB fibre connections.

Conversely, proposals to amend default FLA asset lives and make individual capex proposals a potential price path re-opener are unlikely to make a material difference and could be considered later as part of a wider review. Accordingly, we believe these proposals are better considered further prior to the second regulatory period – if at all - when we have further information and wider review of a particular approach is warranted and possible.

As set out in our submission on the proposed amendments, the Commission already faces a challenging timetable to apply the current IM by December 2021, and to launch further s179 reviews at this stage and issues in parallel can only further undermine delivering on its obligations. The Commission should not be looking to revisit – or entertain proposals to rethink – settled IM positions.

Introduction

1. Thank you for the opportunity to provide feedback on the submissions made on the draft Amendments to Fibre Input Methodologies decision (**the draft**).
2. On 29 and 30 April 2021 the Commission published notices in accordance with section 179 of the Telecommunications Act 2001 (**the Act**) setting out the scope of the potential amendments under consideration, and the proposed process and indicative time frames for considering and consulting on these potential fibre IM amendments.
3. The notices set out a narrow range of proposed amendments:
 - a. To provide for the revised process to determine the initial RAB, comprising a transitional and then later an actual initial RAB. In order to implement this approach, the Commission indicated it would consider amendments to the wash-up, asset valuation, term credit spread and dates by which capex allowances would be set.
 - b. To correct technical errors in formula and some defined terms (**the August amendments**).
 - c. To implement the draft decisions the Commission planned to make to:
 - i. LFC ID requirements to reflect the fact that - due to differing start and end dates - each will have a 2022 disclosure year of different length¹, and to address a practical timing issue relating to the WACC used for disclosure².
 - ii. The Quality Dimensions IM definition of “downtime”, splitting out planned from unplanned downtime.
 - d. To clarify that defined prices and revenues can be applied on a forecast basis, and to clarify the meaning of “income” (the Commission indicated that having considered the matter further, no clarification was necessary)³ (**the November amendments**).
4. Chorus generally supports the Commission’s proposed amendments, and has also proposed a range of additional IM amendments to:
 - a. Change how the Commission valued the “debt” portion of Crown financing⁴ and assumed tax implications of this financing⁵.
 - b. Provide that the IMs wash-up for difference between actual and forecast cost allocator metrics, commissioned assets, and CPI⁶.
 - c. Change the default FLA asset life⁷.
 - d. Provide that disputed connection incentive payments are core capex⁸.

¹ This applies for the purposes of asset revaluations and taxation. See 4.7 and 4.13 of the proposed amendments reasons paper 27 May 2021.

² Reasons paper at 4.17

³ Reasons paper at 5.9

⁴ Chorus submission on November amendments at para 7

⁵ Chorus at para 8

⁶ Chorus submission on August amendments at page 2.

⁷ Chorus on November amendments at page 3

⁸ Chorus on November amendments at page 3

- e. Provide that the current period price-quality path may be “re-opened” when the Commission receives an individual capex proposal (rather than build into the next regulatory period)⁹.
- f. Change how the value of Crown financing is calculated when repayment falls part way through the year¹⁰.
- g. Change the depreciation methodology for newly commissioned assets¹¹.
- h. Change the way costs to upgrade existing connections are treated for capex expenditure purposes¹², and
- i. Require the Commission to recalculate the stranding allowance prior to December 2021¹³.

Comment

Considering Chorus’ proposals would require a specific s179 process

- 5. Chorus’ additional proposals are all substantive changes to how the price quality path will be determined, and none relate to the scope set out in the Commission notification, i.e., to enable a transitional and actual initial RAB setting process and implement planned draft decisions.
- 6. A s179 notice sets out the scope and process for an IM review, it is not an invitation for parties to raise any number of concerns or relitigate settled positions. One of the purposes of s179 notices is to ensure parties are notified of an issue and have an opportunity to fully participate in considering proposed IM changes, this cannot occur when new and unrelated issues and concerns are added to a process that is already underway.
- 7. Accordingly, the Commission should not consider proposals that are not related to the scope of the original s179 notice.
- 8. Therefore, if the Commission did decide to consider Chorus’ proposed amendments, it should set out the scope of the considerations and process in a new s179 notice as required by the Act. Section 179 notices should see to expose the underlying issue and linkages across related IMs, avoiding parties’ incentives to “cherry-pick” review of only some elements that go to an IM position of a particular matter. For example,
 - a. Proposed amendments to the wash-up IM would also need to consider 2Degrees concerns relating to “unlimited” washups and our IM proposals to apply similar wash-up limits to those applying to Part 4 regulated firms, and WACC. The current WACC would be further disconnected from comparator firms that face risks which – in New Zealand – are pushed on to end-users through the wash-up.
 - b. In addition, to the extent the stranding risk is real, the lower-than-expected regulatory cost base and likely future prices, and proposed accelerated depreciate of the FLA (which relates to both core and connection assets contribute) suggests a lower stranding allowance is warranted, if any. Any new consultation should focus on all aspects of the proposal, not the specific amendments proposed by one party.

⁹ Chorus at para 12

¹⁰ Chorus at para 23-24

¹¹ Chorus at 33

¹² Chorus at 39

¹³ Chorus at 46

9. Even if the Commission could consider Chorus' additional amendments in the current process, we do not believe it should. Given the time pressures and other priorities for the December PQ decisions, the process needs to remain focused on finalising the limited number of proposed amendments set out in the notice rather than expanding the scope. Chorus has proposed substantive changes and consideration would be required of related IM settings.

The Commission shouldn't re-visit settled issues

10. In any case, we do not believe that the Commission should consider further amendments prior to making final decisions later this year.
11. Chorus' proposed amendments would imply a substantive change to settled IM settings. However, when we considered each proposal in the table below, a number of the proposals such as the within regulatory period treatment of individual capex proposals and amendments to default FLA asset lives will make no material difference and could be considered in a wider review if at all.
12. Of the substantive matters, the Commission's approach to Crown Financing was considered at length through the IMs process and we are not aware of any fundamental change in the market from when the IMs were completed in October 2020 that suggests a rethink of the stranding allowance is warranted. Customers continue to migrate off poorly performing legacy copper services on to better wireless and fibre alternatives, wireless provides a viable option for many customers who previously had no broadband service, and we continue to see strong growth in UFB fibre connections. We would also be concerned that the proposed continual resetting of the stranding allowance reduces Chorus' incentives to mitigate that risk as the allowance would be driven by the consequences of Chorus' own actions.

Table 1: high level view on proposals

Proposed amendment	Comment
a. Amend Crown financing approach and assumed tax implications	A settled matter that was considered in detail through IMs process – this was a significant and contentious issue ¹⁴
b. Expand wash-up to cost allocator metrics, commissioned assets and CPI	A settled matter. The Commission decided that it would not set out this level of detail in the IMs, this would be left to PQ decisions
c. Change the default FLA asset life	No material difference as Commission can already approve alternative Chorus wants
d. Provide that disputed connection incentive payments are core capex	Disputed expenditure – likely no material difference
e. Individual capex proposals as a price path re-opener	No material difference – there are no expected individual capex proposals that could plausibly result in the claimed cashflow concerns. For example, Chorus refers to connection incentive capex which would comprise around 3% of proposed expenditure in RP1
f. Change how the value of Crown financing is calculated when repayment falls part way through the year	No material difference – first payment is at end of regulatory period
g. Change the depreciation methodology for newly commissioned assets	Approach was determined in IMs

¹⁴ IMs Reasons Paper from 3.172

Proposed amendment	Comment
h. Change the way costs to upgrade existing connections are treated for capex expenditure purposes	No material difference
i. Require the Commission to recalculate the stranding allowance prior to December 2021	Settled position – no real change in context. Chorus largely reiterating arguments made through IM process.

13. We have not considered Chorus’ proposals in detail, including the implications the amendments would have for other IM settings. Chorus is asking that the Commission consider specific elements of the IMs, but there are inevitably wider impacts that would also need to be considered in any new s179 review. Nonetheless, on the face of it, it is difficult not to conclude that Chorus is simply seeking to revisit settled positions. While we would also like the Commission to revisit our concerns with the IM decisions, we appreciate the decisions were only finalised a little over 8 months ago and are still in the process of being implemented.
14. We believe that Chorus’ proposals are better considered – if at all - when we have further understanding of the effectiveness of current IM settings, the future market context, and therefore implications of proposal amendments on wider IM settings. If warranted, the Commission could consider the proposals further prior to the start of the second regulatory period or possibly in the mandated wider review.

Proposed wash-up amendments

15. Submissions also highlight that the draft wash-up amendments may be overly prescriptive for their intended purpose. In particular, while the Commission indicated through the IMs that wash-up settings would be detailed further through PQ decisions¹⁵, the draft amendments suggest a prescriptive IM approach. For example, 2Degrees submits that it does not support the “unlimited” wash-up implied by the proposed amendments, and in our IM submissions we recommended a more nuanced sharing of risk between Chorus and end-users.
16. On the face of it, the proposed amendments go further than necessary to enable a transitional and actual initial RAB setting process and could suggest a detailing of the wash-up that has not been determined. We recommend the Commission review the proposed amendments to ensure they do no more than required to enable the planned draft decision to set a transitional and actual initial RAB. If the Commission wished to consider wider amendments, it would likely need to provide a further s179 notice and consultation.

[End]

¹⁵ See IM Reasons Paper at X41