



Regulatory processes and rules: topic paper

Cross submission | Commerce Commission

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Executive summary

Thank you for the opportunity to comment on submissions on the process and rules IM topic paper.

Scope of the processes and rules IM

Submitters propose that the Commission consider a number of additional input methodologies, ranging from an unbundled services IM, to a pricing methodology, to the implementation of the revenue cap, washup and revenue smoothing requirements. We believe that submissions reflect the importance parties place on input methodologies to promote certainty relating to how Part regulation will apply over time, and beyond the initial 2022 determinations.

However, while we appreciate that the Commission is seeking to balance parties' requests to specify parameters in the regulatory framework with the flexibility it needs to implement Part 6, it remains unclear where in the process these decisions will be made. Accordingly, as set out in our earlier submission, we recommend that the Commission:

- As set out in our earlier submission, provide guidance in its Price Quality Regulation (**PQR**) processes consultation on where (and when) it sees these uncertainties being resolved, ensuring key decisions relating to risk and incentives are aligned across IMs and regulatory decisions. For example, Chorus' IM proposals would see demand and cost risks taken by access seekers and end users, and the approach needs to be reflected in risk and incentive settings; and
- Ensure that weight is given to access seekers' concerns relating to uncertainty over the availability of future services and predictability of future prices by access seekers for their investments. At this stage, there is a risk that the proposed Part 6 implementation leaves key uncertainties for access seekers unresolved.

Reopeners and reconsideration of determinations

In terms of reopening of price quality determinations:

- We support the Commission having the flexibility to clarify or amend regulated services in response to changes in technologies or the market. In terms of practical experience in regulating the technical aspects of telecommunications services, the Commission should look to its Telecommunications Act Part 2 experience where the ability to clarify and amend determinations has been important for the regime; and
- Chorus proposes that capex and opex expenditure be brought together into a single IM. We agree that the regulatory framework should avoid incentives to prefer capex over opex and this could be an opportunity to consider the totex approach further. However, Chorus' proposals cover a range of risks and incentives and would need more consideration than has been available to parties in this consultation.

Introduction

1. Thank you for the opportunity to comment on submissions on the Commission's Fibre Input Methodologies Regulatory Processes and Rules topic paper for implementing Part 6 of Act (**the topic paper**).
2. Submitters generally commented on:
 - a. Additional items that could be included in IMs;
 - b. Pass-through costs; and
 - c. Re-openers and reconsideration of determinations.

Additional items to be included in IMs

3. Submitters have proposed several additional IM areas. Submitters propose that the IMs should specify several addition parameters, including:
 - a. Pricing methodologies to be used to apply cost-based principles it's decisions [Spark];
 - b. The form of price control as, while the first form is set out in the Act, the IMs are intended to apply across regulatory periods which is critical for promoting regulatory certainty [Enable];
 - c. Washup and revenue smoothing design [Chorus, Enable]. 2degrees and Vocus further suggest that the PRIM should specify the wash up mechanism and include specific limits on the washup as the Commission has for Part 4 [page 2];
 - d. PQR evaluation criteria rules, including information requirements, key process, specification of reopeners [Chorus, Enable];
 - e. A consolidated reconsideration of opex and capex to recognise demand changes and specific events [Chorus];
 - f. The regulatory consequences of amalgamations of FFLAS providers [Enable]; and
 - g. The unbundled fibre services, reflecting that the IMs are intended to promote certainty over Part 6 regulation [Vector].
4. While parties seek certainty over different elements of Part 6 regulation – i.e. the translation of costs to revenues, the nature of fibre services and predictability of future prices for those services – they all reflect a desire for more certainty over how Part 6 regulation will apply over time, i.e. beyond the initial BBM parameters. At this stage, there is a risk that the proposed Part 6 implementation leaves key uncertainties for access seekers unresolved.
5. In terms of the specific proposals:
 - a. The ad hoc nature of submitters proposals means there is a risk that the proposals become disconnected from the emerging views and PQR processes consultations. Therefore, as set out in our earlier submission, we recommend that the Commission set out in the PQR processes consultation where it expects key decisions to be made across IMs and Price Quality Determinations (**PQD**);

- b. Chorus proposes that the Act requires an unconstrained washup that washes up all variations between allowed and actual revenue, i.e. that no caps or collars applied [9]. We disagree. The Commission has the discretion to set out how the washup will apply so that it, for example, reflects actual demand or costs incurred;
- c. Submissions highlight that the wash up, revenue cap and revenue smoothing design are important Part 6 outcomes. We agree. The Commission's Part 4 approach and current submissions all suggest that the design of the revenue cap and smoothing is important for achieving Part 6 outcomes. Accordingly, the Commission should provide guidance on its revenue cap, washup and revenue smoothing design; and
- d. Submission highlight that revenue and pricing design parameters - risk/quantity allocation, the washup account, smoothing and permitted depreciation - are related and will need to be considered together. As noted above, the Commission should set out its overall approach in the PQR processes consultation.

Pass through costs

- 6. Chorus further proposes that dispute resolution schemes costs and membership fees be considered pass-through costs. Enable also asks that the Utilities Disputes Limited (**UDL**) levies should be included as a pass-through cost.
- 7. We disagree as these costs are wholly outside the control of the regulated provider. Chorus has choices relating to how it participates in dispute resolution processes and the TCF provides benefits across its regulated and unregulated business. For example, Chorus can withdraw from UDL arrangements in 2026 and Schedule 3C of the Act also provides for the Minister to approve a new disputes scheme. Therefore, Chorus and LFCs can influence these costs, including considering whether the schemes are run in a cost-effective manner (potentially asking the Minister to approve a new scheme) and whether to withdraw from the model in 2026.
- 8. Enable also proposes that audit and verification fees be a recoverable cost for ID purposes. However, the categorisation of costs should align to the PQR proposal process and we recommend the Commission consider this further as part of the processes consultation. For example, if consumer representatives or Commission were to appoint the audit/verification provider and set the scope of the review, then this might rightly be considered a pass-through cost.

Re-openers and reconsideration of determinations

The Commission should reopen for quality and pricing concerns

- 9. Chorus proposes that re-openers should include cyber security and market changes and that a change event should include new government policy such as future tenders. We disagree, it seems likely that the proposed topic paper criteria – the proposed catastrophic or change event criteria – already addresses these events.
- 10. Enable further notes that it does not support the proposal by Trustpower to include an IM process for amending price structures and quality dimensions in response to changes in relevant markets and incentives.
- 11. We disagree. Commission flexibility to clarify and amend regulated services for changes in technology or the market is likely to support the Part 6 purposes. The Commission has rightly looked towards Part 4 for aspects of building block models and, in terms of practical experience in regulating the technical aspects of telecommunications services, it should similarly look to its

Telecommunications Act Part 2 experience. In the Part 2 context, on relatively rare occasions the Commission has usefully clarified or amended determinations to ensure the anticipated regulatory outcomes are achieved and to reduce uncertainty for parties.

12. We further agree with Vocus that the Commission should re-open where information provided to the Commission is materially incorrect and has an adverse impact on end users [para 8]. Vocus' proposed approach better reflects the already strong incentives for access providers to use information asymmetries to influence regulatory outcomes.

Reconsideration of an expenditure allowance

13. Chorus notes that there is no in-principle reason to treat capex and opex differently and proposes to bring capex and opex together into a single IM. Chorus proposes that there be a range of adjustment mechanisms to reflect changes in demand or an event occurs (such as the PSTN migration off copper).
14. We agree that the framework should avoid regulatory incentives to prefer capex over opex (or the reverse), i.e. to avoid inefficient substitution between opex and capex. The Commission raised the possibility in its New Regulatory Framework consultation of applying a total expenditure (totex) framework to the BBM and this could be an opportunity to consider a totex framework further¹.
15. In any case, we haven't considered the range of Chorus adjustments and it's unclear what the wider implications might be for the allocation of risk and incentives that it might lead to. These wider implications would need to be considered further, i.e. as with the proposed approach to washup and revenue smoothing between periods, the risk and incentive implications of within period adjustments also need to be considered in the wider context.

[End]

¹ . Frontier outlines in its report for the AEMC that several jurisdictions have applied the totex framework to mitigate potential inefficiencies in the building block approach.
<https://www.aemc.gov.au/sites/default/files/content/ae0d3fc5-4b9a-496a-a072-50886bc5c86f/2017-12-20-Totex-frameworks-Final-report-STC.pdf>