

Determining Fibre initial regulatory asset bases: Process update

07 April 2022

Purpose

1. To provide interested persons with an update on the process and timing of the remaining decisions that establish the value of Chorus Limited's (**Chorus**) final initial price-quality regulatory asset base (**initial PQ RAB**) and decisions that establish the value of the initial information disclosure regulatory asset bases (**initial ID RABs**) for Chorus and the regulated fibre service providers (**regulated providers**) other than Chorus (**regulated providers other than Chorus**), Northpower Fibre Limited (**Northpower**), Tuatahi First Fibre Limited (**Tuatahi**) and Enable Networks Limited (**Enable**).

Summary

2. This paper sets out the timelines for key process milestones for:
 - 2.1 the remaining decisions that establish the value of Chorus' final initial PQ RAB and our determination of Chorus' opening tax losses for disclosure year 2022;
 - 2.2 the decisions that establish the value of Chorus' initial ID RAB, including the value of Chorus' initial ID-only RAB; and
 - 2.3 the decisions that establish the value of the initial ID RABs for regulated providers other than Chorus and our determination of those regulated provider's opening tax losses for disclosure year 2022.

What is the initial PQ RAB?

3. The collection of fibre assets that Chorus employs in the provision of fibre fixed line access services (**FFLAS**) that are subject to price-quality (**PQ**) regulation is known as its '**PQ RAB**'.¹
4. The PQ RAB is made up of two components:

¹ Clause 2.2.2(1)(b) of *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021. "PQ FFLAS" is defined as "means, in respect of a regulated provider, all FFLAS provided by that regulated provider that is subject to price-quality regulation in regulations made under s 226 of the [Telecommunications Act 2001 (**the Act**)]". *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021, clause 1.1.4(2), definition of "PQ FFLAS".

- 4.1 **Core fibre assets:** fibre assets that are employed by Chorus in the provision of PQ FFLAS (whether or not the asset is also employed in the provision of other services); and
 - 4.2 The **financial loss asset (FLA):** Chorus is treated as owning a FLA that captures unrecovered returns that have accumulated in relation to the Ultra-fast broadband (**UFB**) initiative over the financial loss period (the period starting on 1 December 2011 and ending on 31 December 2021).
5. The initial PQ RAB is the value of the PQ RAB at the commencement of the new fibre regulatory regime on 1 January 2022. This value, once rolled forward for future years, is used as a key input for the second PQ period (**PQP2**) and subsequent regulatory periods. Determining the value of the initial PQ RAB is a critical foundational step for the new regulatory regime, since it underpins the value of Chorus' PQ RAB in subsequent regulatory periods and its value cannot be reconsidered at a later date.

What is an initial ID RAB?

6. The collection of fibre assets that a regulated provider employs in the provision of FFLAS that are subject to information disclosure (**ID**) regulation is known as its '**ID RAB**'.²
7. The ID RAB is made up of two components:
 - 7.1 **Core fibre assets:** fibre assets that are employed by the regulated provider in the provision of ID FFLAS (whether or not the asset is also employed in the provision of other services); and
 - 7.2 The **FLA:** each regulated provider is treated as owning a FLA that captures unrecovered returns that have accumulated in relation to the UFB initiative over the financial loss period (the period starting on 1 December 2011 and ending on 31 December 2021).

² Clause 2.2.2(1)(a) of *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021. "ID FFLAS" is defined as "means, in respect of a regulated provider, all FFLAS provided by that regulated provider that is subject to information disclosure regulation in regulations made under s 226 of the Act". *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021, clause 1.1.4(2), definition of "ID FFLAS".

8. The initial ID RAB is the value of the ID RAB at the commencement of the new fibre regulatory regime on 1 January 2022. This value, once rolled forward for future years, is important to interested persons as it is a major component of the return on investment (**ROI**) calculation under ID, which is a key indicator in assessing whether the purpose of Part 6 of the Act is being met.³ Determining the value of the initial ID RAB is a critical foundational step for the new regulatory regime, since it underpins the value of each regulated providers' ID RAB in subsequent disclosure years and its value cannot be reconsidered at a later date.

What is the initial ID-only RAB?

9. The collection of fibre assets that Chorus employs in the provision of FFLAS that are subject to ID regulation and not PQ regulation is known as its '**ID-only RAB**'.⁴
10. The ID-only RAB is made up of **Core fibre assets**, which are fibre assets that are employed by Chorus in the provision of ID-only FFLAS (whether or not the asset is also employed in the provision of other services).
11. The initial ID-only RAB is the value of the ID-only RAB at the commencement of the new fibre regulatory regime on 1 January 2022. As with the value of the initial ID RAB, this value, once rolled forward for future years, is important to interested persons as it is a major component of the ROI calculation under ID, which is a key indicator in assessing whether the purpose of Part 6 of the Act is being met.⁵ As with the value of the initial ID RAB, determining the value of the initial ID-only RAB is a critical foundational step for the new regulatory regime, since it underpins the value of Chorus' ID-only RAB in subsequent disclosure years and its value cannot be reconsidered at a later date.

³ Under s 186 of the Act, the purpose of ID regulation is to ensure that sufficient information is readily available to interested persons to assess whether the purpose of [Part 6] is being met.

⁴ Clause 2.2.2(1)(c) of *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021. "ID-only FFLAS" is defined as "means, in respect of a regulated provider, all FFLAS provided by that regulated provider that: (a) is subject to information disclosure regulation in regulations made under s 226 of the Act; and (b) is not subject to price-quality regulation in regulations made under s 226 of the Act". *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021, clause 1.1.4(2), definition of "ID-only FFLAS".

⁵ Under s 186 of the Act, the purpose of ID regulation is to ensure that sufficient information is readily available to interested persons to assess whether the purpose of [Part 6] is being met.

Opening tax losses

12. If there are tax losses at the end of the financial loss period (the period starting on 1 December 2011 and ending on 31 December 2021), the opening carry-forward value of the tax losses at the implementation date is calculated by applying a method that sums the annual values of notional deductible interest associated with financing privately funded assets in calculating the UFB tax costs cash flow over the financial loss period.⁶⁷ The inclusion of notional deductible interest in the UFB tax costs cash flow allows for the correct recognition of the timing of the utilisation of losses and changes the closing value of tax losses that is carried forward.⁸
13. As specified in the IMs, opening tax losses for each regulated provider for disclosure year 2022 are a value as determined by us (clause 2.3.3(3)(a)).⁹ This value, once rolled forward for future years, contributes to the calculation of a regulated provider's regulatory tax allowance. The regulatory tax allowance is a significant component of regulatory profit, and therefore, important to interested persons as it is used to determine the ROI calculation under ID, which is a key indicator in assessing whether the purpose of Part 6 of the Act is being met.¹⁰
14. The transitional value of Chorus' "opening tax losses" was used for the purpose of determining the regulatory tax allowance for each regulatory year of its first PQ revenue path (**PQP1**) under clause 3.4.1 of the IMs. The final determination of the value of Chorus' "opening tax losses" for disclosure year 2022 is being made in accordance with clause 2.3.3(3)(a)(i) of the IMs and is important for ID, as described in paragraph 13. The final determination of this value, once rolled forward for future years, will also be used as an input for the regulatory tax allowance used for PQP2 and subsequent regulatory periods.¹¹

⁶ "UFB tax costs cash flow" is defined as "means the tax costs calculated for a financial loss year under clause B1.1.7 of Schedule B". *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021, clause B1.1.2(4)(c) of Schedule B.

⁷ Commerce Commission "Fibre Input Methodologies – Main 2021 amendments – Final decisions – Final reasons paper" (29 November 2021), paragraphs 3.84.3.

⁸ Commerce Commission "Fibre Input Methodologies – Main 2021 amendments – Final decisions – Final reasons paper" (29 November 2021), paragraphs 3.85.

⁹ *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021, clause 2.3.3(3)(a).

¹⁰ Under s 186 of the Act, the purpose of ID regulation is to ensure that sufficient information is readily available to interested persons to assess whether the purpose of [Part 6] is being met.

¹¹ *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021, clause 3.4.1.

Assurance

15. We required Chorus to provide agreed-upon procedures reports produced by an auditor in accordance with ISRS (NZ) 4400 *Agreed-Upon Procedures Engagements*, on the reconciliation of model inputs, used in the calculation of Chorus' PQ RAB estimate, back to Chorus' fixed asset register or to Chorus' financial accounting systems used to prepare general purpose financial reports. We intend to also seek this assurance of figures that are updated from forecasts to actuals in our remaining decisions that establish the value of Chorus' final initial PQ RAB and the decisions that establish the value of Chorus' initial ID RAB.
16. We intend for this reconciliation to include the metrics of capital expenditure, transfers and net book value adjustments (total net value), accounting depreciation, UFB revenues cash flow and UFB operating expenditure cash flow.
17. We expect to obtain reports prepared in accordance with the same standard or a higher assurance standard where source financial information has not been audited, from regulated providers other than Chorus in relation to the decisions that establish the value of their initial ID RABs.

Timing for key process milestones for the remaining decisions that establish the value of Chorus' final initial PQ RAB and decisions that establish the value of Chorus' initial ID RAB

18. We are providing this update to set out the process for the remaining decisions that establish the value of Chorus' final initial PQ RAB as at 1 January 2022 and our final determination of the opening tax losses for Chorus for disclosure year 2022.¹²
19. We will also make decisions that establish the value of Chorus' initial ID RAB as at 1 January 2022 when making the final decisions that establish the value of Chorus' final initial PQ RAB. These decisions will also establish the value of Chorus' ID-only RAB.

Final decision and background of Chorus' transitional initial PQ RAB

20. We made decisions that established the value of Chorus' transitional initial PQ RAB (**transitional initial PQ RAB**) as at 1 January 2022 on 16 December 2021. This served as a key input required to determine the total revenue that Chorus may recover in PQP1, which commenced on 1 January 2022.

¹² Commerce Commission "Fibre Input Methodologies main 2021 amendments: final decisions – Final reasons paper" (29 November 2021), para 3.103. See clause 2.3.3(3)(a)(i) of the *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021.

21. When we determined the value of Chorus' transitional initial PQ RAB, we set out that some information we require to determine the initial PQ RAB value was unavailable at that time (ie, only forecast information for financial loss years 2021 and 2022 was available at the time).¹³¹⁴ We said that once that information became available we will proceed to determine the value of Chorus' final initial PQ RAB in 2022.
22. In respect of the allocation of pre-2011 central office building costs, we also decided:¹⁵
- 22.1 to not accept Chorus' central office space allocation for calculating the pre-2011 central office building costs to be allocated to the initial RAB value and the initial RAB value of core fibre assets as at the implementation date,¹⁶ based on a lack of suitable evidence that Chorus' model and associated data have been assured and certified according to Chorus' assurance framework;¹⁷ and
- 22.2 to allow an allocation equal to 50% of Chorus' proposal to be included in the transitional initial PQ RAB, which reflects the uncertainty around the appropriate allocation given the inadequate assurance and is a conservative estimate of the appropriate allocation (ie, is unlikely to be more than what is in fact attributable to UFB FFLAS). The allocation for the first regulatory period was also reduced to 50% of that proposed.
23. We noted that any difference in the revenue that Chorus would have otherwise been allowed to recover in PQP1 as a result of a change in the value of the initial PQ RAB between transitional and final will be washed-up over PQP2.¹⁸ It is the final initial PQ RAB value that underpins the value of Chorus' PQ RAB in PQP2 and subsequent regulatory periods – the transitional initial PQ RAB value serves only as an input for PQP1.¹⁹

¹³ Commerce Commission "Chorus transitional initial price-quality transitional initial regulatory asset base – Final decision – Reasons paper" (16 December 2021), para 1.8.

¹⁴ Note that the period from 1 July 2021 to the close of the day immediately before the implementation date is considered "financial loss year 2022".

¹⁵ Commerce Commission "Chorus transitional initial price-quality transitional initial regulatory asset base – Final decision – Reasons paper" (16 December 2021), para 5.359.

¹⁶ For clarity, no decision is required with respect to the central office space allocator, which is a default allocator as set out in B1.1.6 of Schedule B of the *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021, but we declined to accept the allocator values and the resulting allocation.

¹⁷ Chorus, "B11 IM Determination Compliance Information" (24 August 2021), slide 4.

¹⁸ Commerce Commission "Chorus transitional initial price-quality transitional initial regulatory asset base – Final decision – Reasons paper" (16 December 2021), para 1.9.

¹⁹ Commerce Commission "Chorus transitional initial price-quality transitional initial regulatory asset base – Final decision – Reasons paper" (16 December 2021), para X9.

Remaining decisions that establish the value of Chorus' final initial PQ RAB

24. To make the remaining decisions that establish the value of Chorus' final initial PQ RAB, we will require Chorus to provide a calculation of its total initial PQ RAB value,²⁰ as at 1 January 2022, that replaces any forecast values with actual values.
25. We will require assurance of the updates from forecast to actual values to be provided. This assurance will be similar to that provided for the actual values that contributed to our decisions on 16 December 2021 that established the value of Chorus' transitional initial PQ RAB as at 1 January 2022.
26. As noted in our final decision that established the value of Chorus' transitional initial PQ RAB:
 - 26.1 Chorus will have the opportunity to provide adequate assurance of the central office space allocation when we decide on the value of the final initial PQ RAB in 2022, which may lead to a change in the amount allocated;²¹ and
 - 26.2 we expected that any further assurance information to support the application of the central office space allocator type would only be available after 1 January 2022.²²²³ This assurance information, once supplied, may necessitate changes to some of the values that will be used to determine the final initial PQ RAB.²⁴
27. We will assess the updated calculation of Chorus' total initial PQ RAB value as at 1 January 2022 that replaces any forecast values with actuals. We will also assess any further assurance of the central office space allocation for calculating the pre-2011 central office building costs that Chorus provides.
28. We expect to make the remaining decisions that establish the value of Chorus' final initial PQ RAB as at 1 January 2022 by July 2022. We will confirm the timing of these final decisions in due course.

²⁰ The "total initial PQ RAB value" is the sum of all of the "initial RAB values" of Chorus' core fibre assets employed in the provision of PQ FFLAS as at the implementation date and the "initial RAB value" of the FLA.

²¹ We also noted that if Chorus does not provide adequate assurance, it is likely that the allocation we allowed for in the transitional initial PQ RBA would remain. See Commerce Commission "Chorus transitional initial price-quality transitional initial regulatory asset base – Final decision – Reasons paper" (16 December 2021), para 5.360.

²² On 25 June 2021 we, under s 221 of the Act, required Chorus to provide any existing documents relating to each of the Property Models, and that documentation, along with a further document submitted in November 2021, was considered as part of determining Chorus' transitional initial PQ RAB.

²³ Commerce Commission "Chorus transitional initial price-quality transitional initial regulatory asset base – Final decision – Reasons paper" (16 December 2021), para 2.10.

²⁴ Commerce Commission "Chorus transitional initial price-quality transitional initial regulatory asset base – Final decision – Reasons paper" (16 December 2021), para 2.10.2.

29. Any differences in the revenue that Chorus would have otherwise been allowed to recover in PQP1 as a result of a change in the value of the initial PQ RAB between transitional and final will be washed-up over PQP2, which will apply from 1 January 2025.

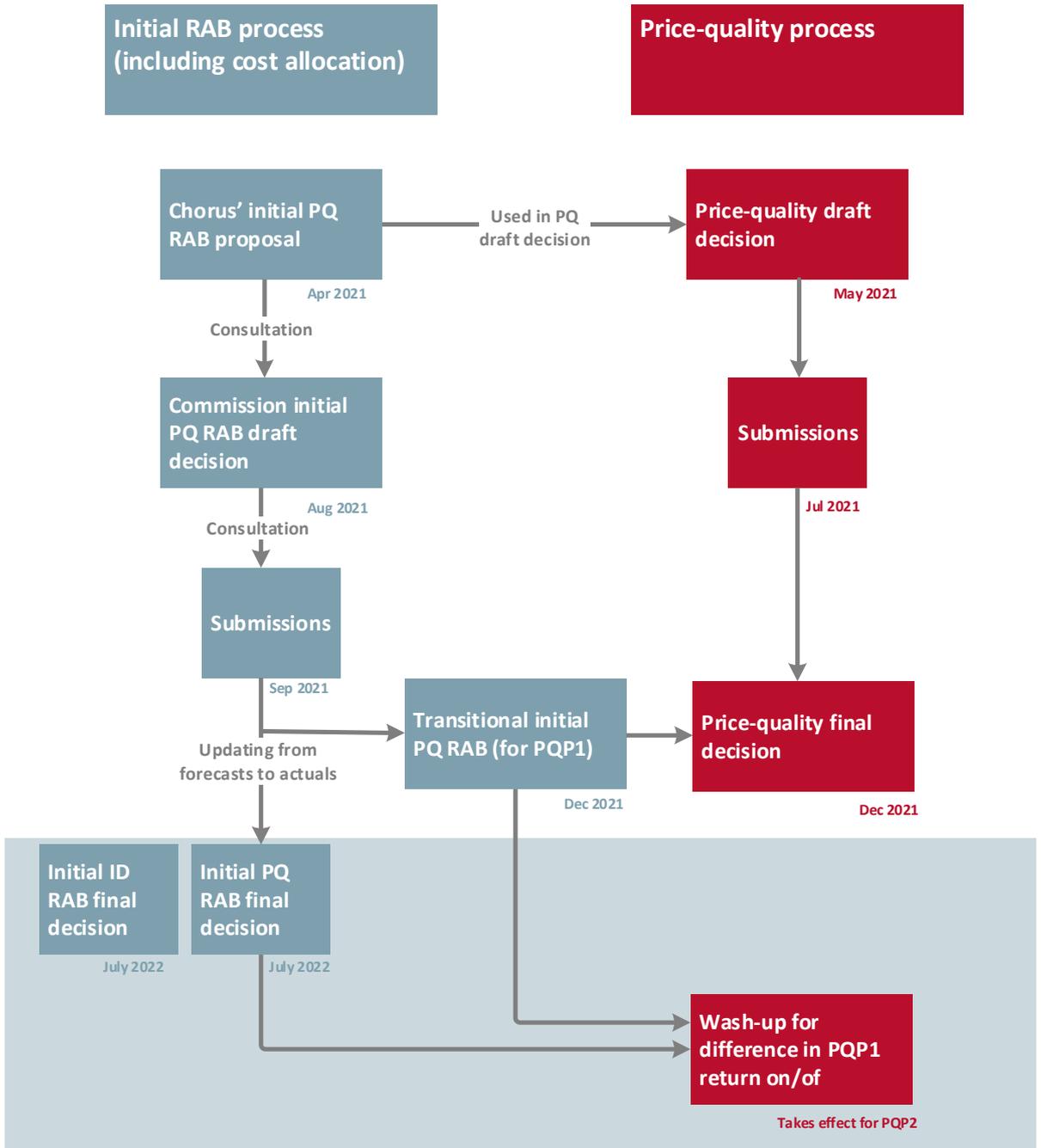
Decisions that establish the value of Chorus' initial ID RAB, including its initial ID-only RAB

30. The decisions that establish the value of Chorus' initial ID RAB, including its initial ID-only RAB, will also be made when we make the remaining decisions that establish the value of Chorus' final initial PQ RAB. Finalisation of Chorus' initial ID RAB is also dependent on replacing forecast values with actual values.
31. The work undertaken in 2021 and the work to be undertaken in 2022 is summarised in Figure 1.1 below.

No further consultation on Chorus' final initial regulatory asset bases (RAB)

32. We will publish the final values of Chorus' initial PQ RAB, initial ID RAB and initial ID-only RAB once our decisions have been made. We expect this to be in July 2022.
33. We will not be undertaking any further consultation on these decisions.

Figure 1.1 Chorus initial PQ and initial ID RAB



Timing for key process milestones for decisions that establish the value of the initial ID RABs for regulated providers other than Chorus

34. We will make decisions that establish the value of the initial ID RABs for regulated providers other than Chorus before their annual disclosures under ID are due for disclosure year 2023.²⁵ These are due no later than 5 months after the relevant end of disclosure year 2023. At the same time as our decisions that establish the value of those initial ID RABs, we will also determine the opening tax losses values for disclosure year 2022 for those regulated providers.²⁶
35. We will follow the steps below when making decisions that establish the value of the initial ID RABs for regulated providers other than Chorus. We expect, in respect of each regulated provider other than Chorus, to:
- 35.1 obtain a proposed calculation of the total initial ID RAB value for each regulated provider in July 2022;²⁷
 - 35.2 review each of the proposed calculation of asset values for each regulated provider, including scrutinising any cost allocators applied;
 - 35.3 use our review to make draft decisions that establish a draft value of the initial ID RABs for each regulated provider in September 2022, including a draft value of each FLA; and
 - 35.4 consult on the draft decisions referred to in paragraph 35.3 in October 2022.
36. We expect to make final decisions that establish the value of the initial ID RABs for regulated providers other than Chorus in late 2022. However, we acknowledge there are risks to this timeline that may affect both the draft and final decision timing, particularly given the potential impacts of Covid-19 on staff availability at the Commission or regulated providers (refer paragraph 42).

²⁵ “For ID-only regulated providers, disclosures required at the end of the disclosure year are not required to be disclosed for 2022 and may be provided at the same time as the 2023 year-end disclosures.” Commerce Commission “Fibre Information Disclosure Final Decisions – Reasons paper” (30 November 2021), para 8.11.5.

²⁶ Commerce Commission “Fibre Input Methodologies main 2021 amendments: final decisions – Final reasons paper” (29 November 2021), para 3.108. See clause 2.3.3(3)(a)(ii)-(iv) of the *Fibre Input Methodologies Determination 2020*, as amended on 29 November 2021.

²⁷ The “total initial PQ RAB value” is the sum of all of the “initial RAB values” of the regulated provider’s core fibre assets employed in the provision of ID FFLAS as at the implementation date and the “initial RAB value” of the FLA.

Fibre information disclosure due dates

37. With the exception of disclosure year 2022, the regulated providers other than Chorus, who are ID-only regulated providers, are required to report annually, no later than 5 months after the regulated provider's disclosure year-end, various reports in respect of the relevant disclosure year.
- 37.1 For disclosure year 2022,²⁸ an ID-only regulated provider must complete and publicly disclose the required reports no later than 5 months after the end of disclosure year 2023.
38. The regulated providers other than Chorus will therefore provide the required reports, with information dated from 1 January 2022 to the end of their disclosure year, no later than 5 months after the regulated provider's disclosure year-end. The deadlines for this reporting are shown in the table below.

ID-only regulated provider	Balance date (same as Disclosure year-end)	ID deadline for disclosure year 2022	ID deadline for disclosure year 2023
Northpower	31 March	31 August 2023	31 August 2023
Tuatahi	31 March	31 August 2023	31 August 2023
Enable	30 June	30 November 2023	30 November 2023

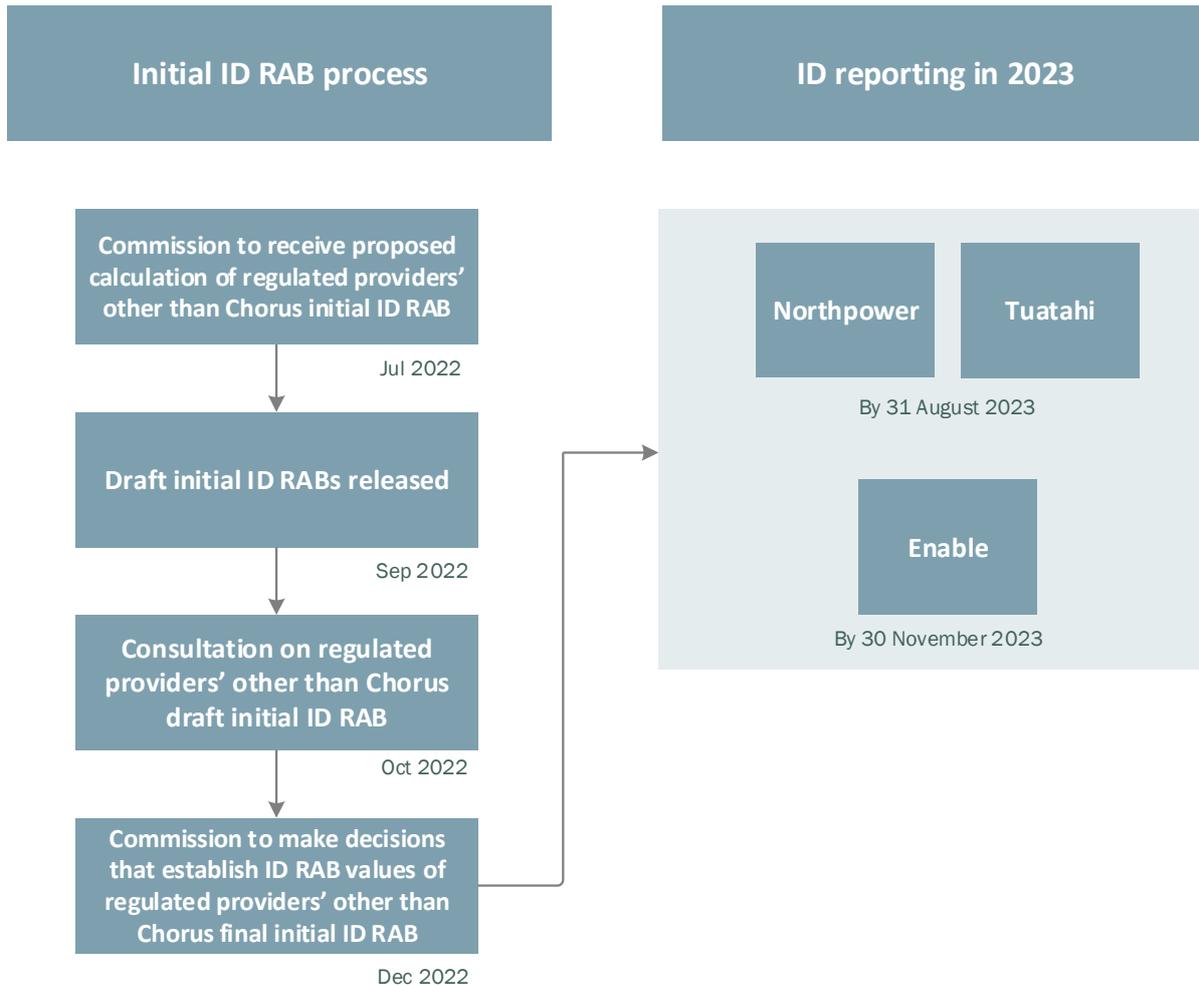
How our updated initial ID RAB process fits with our ID reporting process

39. Each of the regulated providers other than Chorus are required to provide their first ID disclosures in 2023.
40. As noted above, the reporting for the 2022 disclosure period will also be supplied by regulated providers at the same time as they provide reports for the 2023 disclosure year.

²⁸ The start of disclosure year 2022 for each ID-only regulated provider does not coincide with the commencement date of the regulation. To ensure each ID-only regulated provider can apply information disclosure requirements from the commencement date to the end of disclosure year 2022 (the 'disclosure period'), it is therefore necessary to 'pro-rate' or limit those requirements so they are interpreted and applied on the basis of a disclosure period rather than on the basis of a disclosure year.

- 41. As LFCs must provide disclosures no later than 5 months after the end of each disclosure year, the earliest reports are due from the regulated providers other than Chorus by 31 August 2023.
- 42. We intend to make final decisions that establish the value of the initial ID RAB for each regulated provider other than Chorus by the end of December 2022.²⁹

Figure 1.2 Initial ID RAB process for regulated providers other than Chorus and ID reporting in 2023



²⁹ At the time of preparing this process update, the impacts of Covid-19 on the Commission and regulated providers is still uncertain. In the event that completion by 31 December 2022 isn't feasible (for example, due to Covid-19 impacts) then decisions may push out into Q1 2023. We will also consider staggering our final decisions if necessary. However, even if delays are encountered due to Covid-19, we intend to have made final decisions for all regulated providers other than Chorus no later than 31 March 2023.