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Tricia Jennings
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Commerce Commission
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BY EMAIL ONLY

Dear Tricia,

RE: CONSULTATION PAPER – NETWORK FOOTPRINT AND DEMAND, UCLL AND UBA PRICING REVIEW DETERMINATIONS

Vodafone welcomes the opportunity to comment on the Commission's consultation paper concerning network footprint and demand for the UCLL and UBA pricing review determinations, released on 21 September 2015.

This letter (our submission) should be read along with the expert reports by WIK-Consult and Network Strategies that respond to the same Commission consultation paper.

The first best solution is to obtain information from Chorus and all other providers of fixed lines (eg LFCs) to create an accurate picture of every fixed line's location (within the TSO). This represents current demand and so represents the connections the HEO's network should be dimensioned to connect (before any demand growth in subsequent years). The gap between locations for network premises and assumed customer demand must be 0%. Any adjustment should not be necessary.

We fully support the analysis carried out by WIK-Consult and Network Strategies, and share the conclusions reached. Thus as a second best approach, we support WIK-Consult's and Network Strategies' recommendation that the Commission should make no further adjustment to the 3.6% gap. This is based on the most reliable information available to it.

To introduce an adjustment based on a third, and differently sourced, dataset simply introduces further inaccuracies to the Commission's approach.

The Commission proposes a demand adjustment

The Commerce Commission is consulting on whether the 'gap' between the UCLL network footprint and demand should be adjusted.

The gap is currently 3.6% and the Commission is considering an adjustment that would result in a gap of 7.5%, which corresponds to Statistics New Zealand's estimate of the proportion of empty dwellings.

The stated purpose is to ensure paying customers support the costs of the connections for unoccupied buildings.

A gap should not exist

We agree with the Commission: the modelled network should not be dimensioned for address points that do not represent demand.

The Commission is attempting to reconcile two sets of data: from Corelogic on address points and from Chorus on line demand. The Commission has attempted to remove vacant buildings from the CoreLogic database.

However Vodafone believes that there should be no gap between the connections modelled for the UCLL network and the demand denominator for the final per line cost allocation calculation. This point has been made previously by WIK-Consult:[1]

> *We repeatedly have argued that ideally, the appropriate network footprint of the HEO should cover 100% of actual demand, not more and not less. There should be no difference, if the data is accurate, between the number of connections over which the total modelled cost should be spread and the number of connections which determines the footprint of the network.*[2]

And, as advised by WIK in August 2015:[3]

> *If the HEO's network covers a larger footprint than the one determined by actual demand, the incremental costs of covering the difference in demand has to be regarded as an investment which the HEO undertakes to meet the difference between potential and actual demand with a certain probability. The cost and risk of that incremental investment should be covered by the HEO and the potential revenues of potential demand. It is inappropriate that actual demand has to cover those costs. This holds in particular under the constant demand assumption of the Commission."*

The gap is a conceptual error in the model that risks loading the costs of an over-dimensioned network on existing customers. As such, we support the Commission's attempt to correct the UCLL network footprint by removing address points that belong to vacant sites.

If a gap exists, it must reflect New Zealand's demographics/characteristics

Local lifestyle and cultural factors are characteristics that will impact on the number of empty buildings. Features of New Zealand's fixed line services (such as free local calls) will also impact on incentives to install a fixed line in an occasionally used building such as a holiday bach.

However we recognise that these characteristics should already be inherent in the CoreLogic and Chorus data, and so any further adjustment should not be necessary.

Adjustment using Statistics New Zealand data does not lead to a reliable estimate

It is not surprising that, given the information on vacant sites is taken from a third source - Statistics New Zealand - that the adjustment does not result in a perfect match between the CoreLogic and Chorus datasets.

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[1] WIK-Consult, Submission of 6 October 2015 on Demand.

[2] See also similar arguments made by Spark, Submission of 13 August 2015, para. 110ff.

[3] WIK-Consult, Submission of 12 August 2015, para. 353.

As explained by Network Strategies, due to definitional issues the Statistics New Zealand data is inappropriate for use in this particular situation. This is because:

- An introduced bias due to the classification of holiday homes as 'empty';
- Many such empty dwellings would be outside the TSO boundary;
- A number of 'empty' dwellings will have a fixed line that is billed to a customer; and
- The proposed adjustment is inappropriate when considering vacancy rates in business (including retail) premises.

A 7.5% adjustment would be a substantial overestimate of vacant dwellings and buildings

We agree with Network Strategies' conclusion that:[4]

> *the proposed 7.5% adjustment would over-estimate the proportion of empty dwellings and buildings (without revenue-earning fixed lines) within the Commission's network footprint, and would increase the error associated with the resultant estimated prices.*

We also fully agree with Network Strategies' recommendation that the Commission retain a gap of 3.6% without any further adjustment.

If an adjustment is to be made, this must be reflected in network dimensioning

We support WIK-Consult's recommendation that, in the case that the Commission does choose to make an adjustment this must also be reflected in the network footprint:[5]

> *If the Commission intends to adjust to achieve a certain gap it has to adjust its network footprint. We conceptually reject the need to normalise the data to any particular point as a necessity for the reasons set out above. The level of actual demand is a hard fact based on actual operator data. It is inappropriate in our view to artificially adjust it. Instead, only if there was strong and reliable evidence to support it, and only for consideration as a third best adjustment, the Commission would have to expand the network footprint from a 3.6% gap to a 7.5% gap.*
>
> *We acknowledge that the approach developed [above] sounds as arbitrary as the one proposed by the Commission. In fact, it is more methodologically sound. The difference is that this approach addresses the problem (if there is one) directly at the point where it occurs and does not lead to an additional compensating distortion.*

Vodafone's response to the Commission's specific consultation questions is included as **Appendix 1.**

Warm regards,

Tamara Linnhoff
Senior Analyst, Public Policy
Vodafone New Zealand Limited

[4] Network Strategies, Submission of 6 October 2015 on Demand.

[5] WIK-Consult, Submission of 6 October 2015 on Demand.

APPENDIX 1 – THE COMMISSION'S CONSULTATION QUESTIONS

Question 1: Do you agree that a 3.6% gap between the UCLL footprint and demand is too small, and an adjustment should be made?

A 3.6% gap is not too small. No further adjustment should be made.

Question 2: We have Census data that suggests that the gap between the UCLL footprint and demand is closer to 7.5%. Do you support this statistic? Do you have any other data sources that support a different gap?

We do not support the use of Statistics New Zealand census data for the proposed adjustment.

This is for reasons including:

- the introduced bias due to the classification of holiday homes as 'empty';
- many holiday homes lie outside the TSO boundary;
- some 'empty' dwellings will have an operational fixed line; and
- the proposed adjustment is inappropriate when considering vacancy rates in business (including retail) premises.

The Commission should rely on the corrected CoreLogic data base.

Question 3: Do you agree with our proposed adjustment to demand? Do you have any alternative methods for implementing a gap between footprint and demand?

We do not support the proposed adjustment to demand.

The proposed adjustment is methodologically incorrect, because:

- the proposed 7.5% adjustment will substantially over-estimate the proportion of empty dwellings and buildings (that do not contain revenue-earning fixed lines) within the Commission's network footprint; and
- would, therefore, increase the error associated with the resultant estimated prices.

The right solution is to obtain information from Chorus and all other providers of fixed lines (eg LFCs) to create an accurate picture of every fixed line's location (within the TSO). These are the connections the HEO's network should be dimensioned to connect. The gap between locations for network premises and assumed customer demand must be 0%. Any adjustment should not be necessary.

As a second best approach, we support WIK-Consult's and Network Strategies' recommendation that the Commission should make no further adjustment to the 3.6% gap. This is based on the most reliable information available to it.

To introduce an adjustment based on a third, and differently sourced, dataset simply introduces further inaccuracies to the Commission's approach.