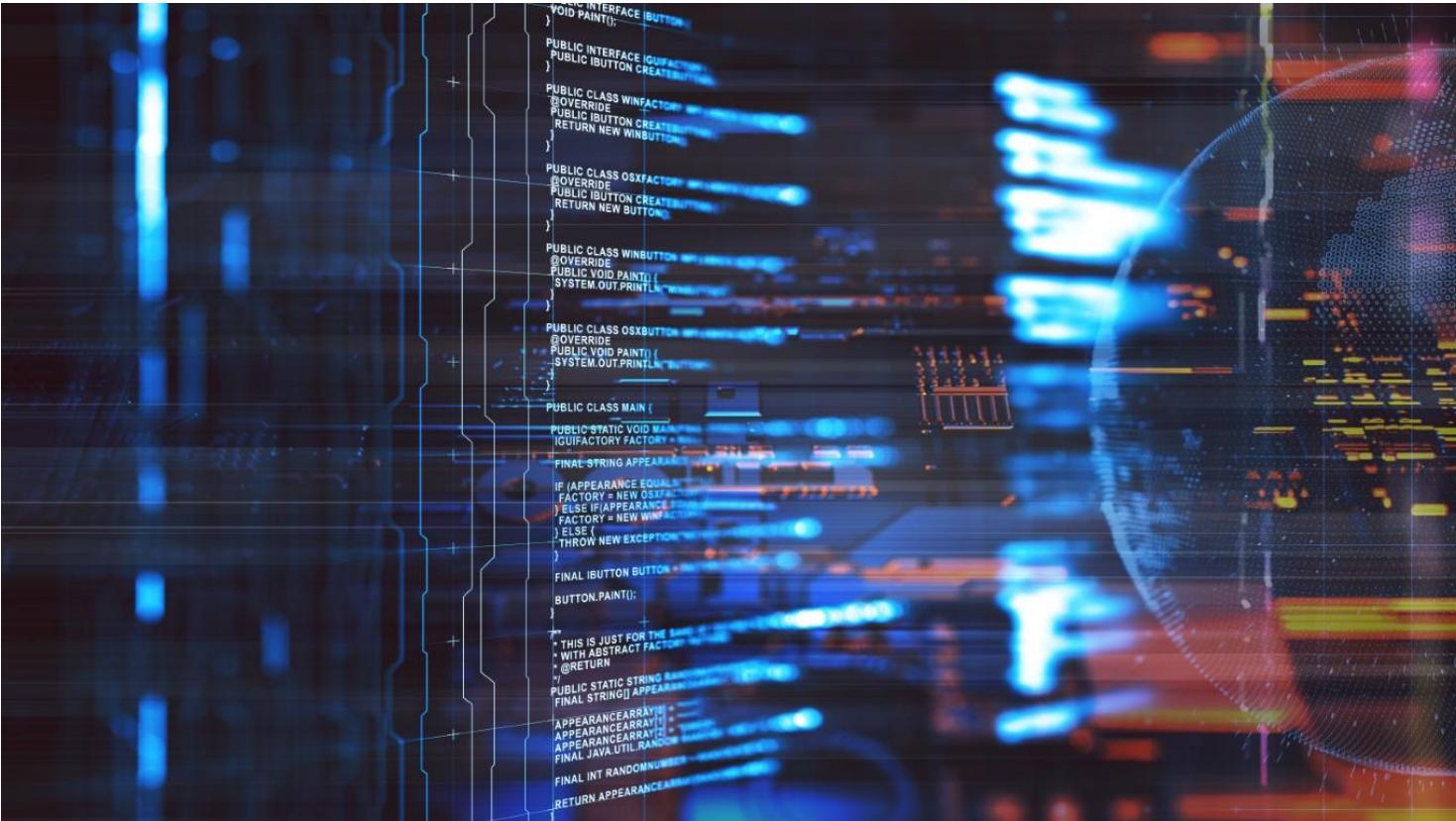


Cross-submission in response to the Commerce Commission’s fibre regulation – Regulatory processes and rules paper

16 September 2019



OVERVIEW

- 1 This cross-submission responds to submissions on the Commerce Commission’s consultation paper *Fibre input methodologies – Regulatory processes and rules – topic paper* published on 19 August 2019 (**P&R Paper**).
- 2 The purpose of input methodologies (**IMs**) is to provide certainty and clarity of the rules that apply in setting price-quality regulation across regulatory periods. The overall theme from submitters is that it’s important the Commission addresses uncertainty about the transition to a new regulatory framework by delivering certainty through the processes and rules IM (**P&R IM**).
- 3 We appreciate the opportunity to provide our views on other parties’ submissions. This cross-submission does not attempt to address all the arguments raised in submissions but seeks to cover key themes and issues of particular importance.
- 4 A number of the matters raised by submitters have already been set out at length in our earlier submissions. We set out in the **Appendix** references to the sections of our submissions which address these points.

Areas of alignment in submissions

- 5 There is alignment amongst submissions on a number of topics raised in the Commission’s P&R Paper. For example:
 - 5.1 **Revenue smoothing** – Agreement that guidance on revenue smoothing is needed in the P&R IMs and that it should be considered together with other mechanisms.¹
 - 5.2 **Expenditure evaluation processes** – Support for expenditure information, evaluation processes and criteria to be set in IMs before price quality determinations (**PQDs**) for certainty in the regime.²

¹ Enable and Ultrafast (9 September 2019), *Submission on NZCC Fibre Regulation Input Methodologies Regulatory Process and Rules*, at [3.8]; Spark (9 September 2019), *Regulatory processes and rules: topic paper*, at [17], [20].

² Enable and Ultrafast (9 September 2019), *Submission on NZCC Fibre Regulation Input Methodologies Regulatory Process and Rules*, at [6.1]-[6.9]; Vocus (9 September 2019), *Fibre Input Methodologies – Regulatory processes and rules Submission to the Commerce Commission*, at [19]-[21].

- 5.3 **Pass-through and recoverable costs** – General agreement amongst submitters³ with the proposed approach to pass-through and recoverable costs. Other local fibre companies (**LFCs**) also agree that costs associated with disputes resolution schemes should be included as pass-through costs.
- 5.4 **Reconsideration of expenditure allowance** – A submitter recognises that the pace of change in the telecommunications sector – notably technologies and services – may require specific treatment under Part 6 of the Telecommunications Act (**Part 6**).⁴ This aligns with our view⁵ that the uncertainties we expect to face are different to Transpower’s and other Part 4 of the Commerce Act (**Part 4**) utilities (who have fully built networks, longer-lived assets and a slower pace of market and technological change). The IMs should include mechanisms to efficiently manage risk and uncertainty – including allowing us to access additional capex within a regulatory period. Locking in a fixed allowance for a regulatory period could leave regulated suppliers unable to invest in initiatives that provide consumer benefit.
- 5.5 **Balance dates** – Information disclosure (**ID**) balance dates for each regulated supplier could align to their financial reporting balance dates for efficiency (including reduced compliance costs).⁶

Our response to matters others have raised

- 6 Some submissions raise issues that are incorrect or outside the scope of the IMs, for the reasons explained below.

Wash up

- 7 While there was broad alignment that the wash-up mechanism needed to be specified upfront in the IMs, some submitters suggest that in line with Part 4, there should be

³ Enable and Ultrafast (9 September 2019), *Submission on NZCC Fibre Regulation Input Methodologies Regulatory Process and Rules*, at [2.2]-[2.7]; Northpower (9 September 2019), *Submission on: Fibre input methodologies Regulatory processes and rules Topic paper*, p2; Vector (9 September 2019), *Submission: fibre input methodologies regulatory processes and rules topic paper*, p3.

⁴ Spark (9 September 2019), *Regulatory processes and rules: topic paper*, at [23].

⁵ See Chorus (9 September 2019), *Submission in response to the Commerce Commission’s Fibre input methodologies – Regulatory processes and rules topic paper*, [53] – [57]; Chorus (16 July 2019), *Submission in response to the Commerce Commission’s fibre regulation emerging views dated 21 May 2019*, at [332] – [340].

⁶ Enable and Ultrafast (9 September 2019), *Submission on NZCC Fibre Regulation Input Methodologies Regulatory Process and Rules*, at [5.1]-[5.4]; Northpower (9 September 2019), *Submission on: Fibre input methodologies Regulatory processes and rules Topic paper*, p2-3.

limits applied to the wash-up.⁷ We note that not all Part 4 businesses face constraints on their wash-up, for example, Transpower's IPP wash-up has no limits. Our interpretation is that the Telecommunications Act (**Act**) requires an unconstrained, symmetric wash-up and the Part 4 constraints are not available in the current legislation for the first regulatory period (**RP1**).

- 8 There is also rationale for a symmetric wash-up to continue to apply into future regulatory periods. As mentioned previously,⁸ a wash-up mechanism is important in this regime given the range of additional mechanisms (anchor and mandatory services, and geographic consistent pricing) carried over in contrast to other regimes. These constrain Chorus' revenue and may lead to periods of under-recovery of allowable revenues and without an ability to carry under-recovery into future periods, real financial capital maintenance (**FCM**) will not be realised.
- 9 This highlights why it is important for the Commission to give stakeholders clarity and confirm in a P&R IM that the Act requires an unconstrained, symmetric wash-up. This will help address the growing uncertainty amongst stakeholders as to how key mechanisms will work together in the regime.

Reopeners

- 10 Some submitters⁹ comment that the proposed 'false and misleading' reopener is not broad enough or requires another threshold of 'materially incorrect'. Chorus supports this reopener without the changes suggested by these submitters. The 'error' event reopener addresses their comments.
- 11 We don't agree with the view that a reopener mechanism should be used to adjust the price-quality path if our actual capital and/or operating expenditure is below the levels in our proposals and allowed for in the price-quality path.¹⁰ This would prevent us from outperforming expenditure allowances through efficiency gains, which is a key incentive inherent in ex-ante regulation. It would imply that variance between forecast and actual capital expenditure means the forecast was 'incorrect'. Out-performance is encouraged in a building block model (**BBM**), and is not incorrect.

⁷ 2degrees (9 September 2019), *Submission on Commerce Commission Regulatory Processes and Rules Input Methodology Topic Paper*, p2; Vocus (9 September 2019), *Fibre Input Methodologies – Regulatory processes and rules Submission to the Commerce Commission*, at [3].

⁸ Chorus (9 September 2019), *Submission in response to the Commerce Commission's Fibre input methodologies – Regulatory processes and rules topic paper*, at [9]-[13].

⁹ 2degrees (9 September 2019), *Submission on Commerce Commission Regulatory Processes and Rules Input Methodology Topic Paper*, p1; Vocus (9 September 2019), *Fibre Input Methodologies – Regulatory processes and rules Submission to the Commerce Commission*, at [8]-[9].

¹⁰ 2degrees (9 September 2019), *Submission on Commerce Commission Regulatory Processes and Rules Input Methodology Topic Paper*, p1.

- 12 We have suggested that there should be re-openers for events related to cyber security and market changes. In contrast to a broad reopener for any variances between forecast and actual expenditure, our proposal is for reopeners with carefully defined trigger events that recognise that the dynamic nature of the telecommunications sector may require in-period adjustments to expenditure that could not have been foreseen prior to commencement of the regulatory period.

Service specifications and future prices

- 13 One submitter suggested that IMs need to provide certainty over service specifications and future prices. It isn't the role of IMs to provide such certainty. This suggestion is at odds with the revenue cap and anchor services model prescribed in the Act. In effect it is a request that the Commission replicate the legacy Part 2 Standard Terms Determination (**STD**) model within the new fibre regulatory framework.
- 14 In our cross-submission on the Emerging Views Paper (**EV Paper**) we acknowledged retail service providers' (**RSPs**) concerns with future uncertainty at this stage around non-price terms when the NIPA falls away as we enter the new regime.¹¹ But we are moving to an incentives-based framework, which is a deliberate departure from previous regimes involving detailed prescription of both price and non-price terms. Individual price and non-price terms will be baselined by anchor service and direct fibre access service (**DFAS**) regulations. The existence of anchor service and DFAS regulations is evidence that an STD like regime is not intended under the new fibre regulatory regime. The anchor service and DFAS regulations would have no role to play in a framework where the Commission imposes detailed constraints on price and non-price terms across the fibre service portfolio.
- 15 Detailed prescriptive terms would also give rise to all the problems with excessive constraint we described in previous submissions.¹² The submission effectively acknowledges this by saying the Commission should be able to adjust these within a regulatory period. This would be overly cumbersome and would deny Chorus the opportunity to innovate or respond to changing consumer demands in a timely way.

¹¹ See Chorus (31 July 2019), *Cross-submission in response to the Commerce Commission's fibre regulation emerging views*, at [9.13].

¹² See Chorus (16 July 2019), *Submission in response to the Commerce Commission's fibre regulation emerging views dated 21 May 2019*, at [246] –[252]; Chorus (21 December 2018), *Submission in response to the Commerce Commission's invitation to comment on its proposed approach to the new regulatory framework for fibre dated 9 November 2019*, at [214]-[216].

APPENDIX: SUMMARY POSITIONS – RESPONSE TO SUBMISSIONS

- 16 Other submissions to a large extent raise arguments we have already responded to in our submissions. Rather than repeat our responses, we provide the following summary of Chorus’ positions on key issues, with a cross-reference to where our view is explained in detail.

Issue	Chorus position	Previous Chorus submission reference
<i>Legislative framework</i>	<p>There is general agreement between RSPs and LFCs the scope of P&R IMs is to provide the upfront rules that then apply to price-quality regulation (PQR). Submitters agree is that it’s important to a new regulatory framework to provide certainty through the P&R IM.</p> <p>Section 166(2) does not require the Commission to depart from outcomes that would occur in workably competitive markets, and section 162 (purpose statement of Part 6) has primacy over section 166(2)(b).</p>	<p>21 December 2018 [81]-[97], [144]-[147].</p> <p>16 July 2019 [56]-[63].</p> <p>9 September 2019 [6]-[8]</p>
<i>Wash up</i>	<p>The wash-up mechanism is specified in the Act, and a number of submitters agree it is therefore appropriate to include the requirement in the IMs. Our interpretation of the legislation is clear that:</p> <ul style="list-style-type: none"> • The application of a systematic wash-up account for RP1; and • The wash-up account is unconstrained (i.e. no caps or collars applied) and it washes up all variation between allowed and actual revenue. <p>There are good reasons for a symmetric wash-up to continue to apply into future regulatory periods.</p>	<p>21 December 2018 [117]-[118], [148].</p> <p>1 February 2019 [21.2], [75]</p> <p>16 July 2019, Appendix A [27]-[30].</p> <p>31 July 2019 [57]</p> <p>9 September 2019 [9]-[13].</p>
<i>Revenue smoothing</i>	<p>Submitters agree guidance on revenue smoothing is needed in the P&R IMs. We support that revenue smoothing between regulatory periods should be included in the P&R IMs, because:</p> <ul style="list-style-type: none"> • A balance needs to be struck between revenue smoothing to ease price shocks and the need for cost recovery. • The Commission in its EV Paper put forward a number of depreciation options for smoothing revenues, these issues all need to be considered together. 	<p>21 December 2018 [228.2].</p> <p>16 July 2019, Appendix A [35]-[36].</p> <p>9 September 2019 [14]-[17].</p>

<i>Price-quality evaluation criteria</i>	<p>Submitters support evaluation criteria being set in IMs before price quality determinations for certainty in the regime.</p> <p>We support expenditure evaluation criteria should be specified in IMs so they are clear when formulating a price quality proposal.</p>	<p>21 December 2018 [236].</p> <p>16 July 2019, Appendix A [328]-[331], [341]-[347]</p> <p>9 September 2019 [18]-[25].</p>
<i>Price-quality processes</i>	<p>Submitters support for expenditure information and evaluation processes being set in IMs.</p> <p>We consider the fundamental principles and information required for the price quality processes should be specified in IMs not PQD as certainty is needed.</p>	<p>21 December 2018 [67-75], [232]-[235].</p> <p>16 July 2019, Appendix A [308]-[321]</p> <p>9 September 2019 [26]-[33].</p>
<i>Pricing IM</i>	<p>There is no justification for a pricing IM as we are subject to a revenue cap to constrain our return across our product portfolio and a number of other pricing constraints.</p>	<p>31 July 2019 [15]-[26].16 July 2019, Appendix A [97]-[99].1 February 2019 [22]-[27], [55]-[59].21 December 2019 [128].</p>
<i>Unbundling IM</i>	<p>An unbundling IM is not required, nor in fact permitted to the extent that it seeks to elaborate on requirements not in Part 6.</p>	<p>31 July 2019 [27].1 February 2019 [8.1], [48]-[51].</p>
<i>Form of control</i>	<p>The form of control is set by legislation for RP1 as a revenue cap.</p>	<p>16 July 2019 [51].</p> <p>1 February 2019 [27], [56].</p> <p>9 September 2019 [37.1].</p>
<i>Reopeners</i>	<p>Telecommunications-specific scenarios should be added to the list of reopener matters, including for events relating to cyber security and market changes.</p>	<p>1 February 2019 [21].</p> <p>16 July 2019, Appendix A [332.2], [348]-[351].</p> <p>9 September 2019 [48]-[50].</p>
<i>Reconsideration of expenditure allowance</i>	<p>A submitter recognises that the pace of change in the telecommunications sector requires specific treatment under Part 6. We agree that further mechanisms should apply in Part 6 to address these risks and uncertainties.</p>	<p>21 December 2018 [230].</p> <p>1 February 2019 [21].</p> <p>16 July 2019, Appendix A [332]-[340].</p> <p>9 September 2019 [51]-[56].</p>
<i>Pass-through and recoverable costs</i>	<p>There is general agreement amongst submitters with the proposed approach to pass-through and recoverable costs. We support an approach in line with Part 4 categorising of costs as pass-through and recoverable costs. Costs associated with disputes resolution schemes and membership fees should be included as pass-</p>	<p>21 December 2018 [229.3].</p> <p>16 July 2019, Appendix A [332.4]</p> <p>9 September 2019 [38]-[46].</p>

	<p>through costs, and recoverable costs should allow for innovative practices and some insurance related costs.</p> <p>Clarity is needed on how levies associated with the implementation of the new regulatory regime will be treated as a significant proportion of these will be paid prior to the implementation date.</p>	
<i>Regulatory balance dates</i>	<p>LFCs agree that ID balance dates for each regulated supplier could align to their financial reporting balance dates for efficiency (including reduced compliance costs).</p> <p>There is also precedent for different balance dates for each regulated supplier and it is best if most suppliers regulated for ID have the same balance date (e.g. 30 June).</p>	9 September 2019 [58]-[63].