



10 March 2006

Transpower Post-Breach Inquiry
Network Performance Group
Networks Branch
Commerce Commission
PO Box 2351
WELLINGTON

BY EMAIL: electricity@comcom.govt.nz
cc Douglas Webb

Dear Paula

Cross-Submission on the Commerce Commission's Intention to Price Control Transpower

1. TelstraClear welcomes the opportunity to make a cross-submission in relation to whether or not the Commerce Commission should place Transpower under price control.
2. As we noted in relation to the Unison price control inquiry, TelstraClear would not normally make submissions in relation to matters relating to regulation in network industries outside of telecommunications, but we consider there is substantial commonality of issues in relation to whether to price control electricity lines business (such as Unison and Transpower) and the designation of various services under the Telecommunications Act (notably, fixed-to-mobile termination rates and local loop unbundling). For the sake of regulatory certainty and stability, it is important that the Commission is as consistent as possible (taking into account industry specific factors and differences in the regulatory regimes).
3. In our submission in relation to the Unison price control inquiry we applauded Commission for the consistency between the approach taken in that inquiry and on the matter of whether to designated fixed-to-mobile termination rates. Having reviewed the Commission's consultation paper on its intention to place Transpower under price control, and the submissions that have been made in response to it, we have question marks as to whether the approach that the Commission has taken is as consistent as it should be, both with other Part IV/Part IVA of the Commerce Act investigations, and with investigations the Telecommunications Act. These concerns relate to:
 - a. The Commission's failure to apply a building block approach to determining whether prices are excessive; and

- b. More importantly, the Commission's quantitative evaluation of the impact of price control on future investment by the regulated utility.

Building block approach

4. A large number of the submissions (including Transpower) were critical of the Commission for not applying a building block approach to determining whether Transpower's prices were excessive. TelstraClear shares these concerns.
5. The Commission normally applies a building block approach to the determination of what the efficient level of a utility's costs would be, and therefore whether their prices are excessive. This is an important part of the Commission's quantitative assessment of the net benefits of regulation.
6. However, for the Transpower price control inquiry the Commission has not taken this approach (page 6):

"The Commission's approach to develop a "factual" for Transpower differs from that taken in the recent intention to declare control of Unison Networks Limited. In that intention, the Commission undertook a "building blocks analysis" to construct a number of possible future price paths (i.e., factual scenarios) to compare with Unison's own projections of its prices over the next few years (i.e., counterfactual scenarios). In Transpower's case, the Commission does not consider that such an analysis would be feasible until it is known which elements of Transpower's plans for future investments are to proceed." (emphasis added)

7. TelstraClear does not find this argument compelling. In any investigation there will be uncertainty over whether future investments should/would proceed/will be efficient. Transpower is no exception. In telecommunications (be it fixed line or mobile) – in which technological change is much more rapid than in electricity transmission – we would expect there to be much more uncertainty, yet the Commission has not shied away from application of a building block approach in its Telecommunications Act investigations.

Quantitative evaluation of the impact of price control on future investment

8. While the Commission was reluctant to apply a building block approach to the assessment of efficient costs, because of uncertainty about future investment, it nevertheless:
 - a. assessed that the vast majority of the benefits of price control would come from improved investment decisions; and
 - b. calculated these benefits on the basis that (i) Transpower would go ahead with its proposed major investments (notably on the HVDC link, and on the Whakamaru-Otahuhu 400kv line); and (ii) these investments would occur 1-3 years later than Transpower planned (providing substantial benefits because of the time value of money) and at lower cost than Transpower projected.

9. Leaving aside that the Commission could have applied these assumptions to a building block approach, we find this assessment to be rather interesting in the context of the Commission's investigations of whether to regulate unbundling of Telecom's local loop network, and Telecom's and Vodafone's fixed-to-mobile termination rates.
10. In the case of Transpower the Commission has assessed that price control/regulation would result in substantial benefits from improving the efficiency in future network investment. However, in the case of the Commission's investigations under the Telecommunications Act the Commission has expressed concern about the exact opposite. TelstraClear is unable to reconcile this. If the Commission's assessment is correct in its Transpower assessment then this would suggest to TelstraClear that the Commission has substantially understated the net benefits of regulation of local loop unbundling and fixed-to-mobile termination rates, and over-stated the negative impact that designation of these services could have on dynamic efficiency. This conclusion is certainly consistent with the submissions that TelstraClear has made in the past in which we have argued that designation of LLU and fixed-to-mobile termination rates would be likely to promote efficient investment – it would facilitate new investment by access seekers, which in turn would force the incumbent(s) to invest in order to compete.
11. The alternate is that the Commission's approach was correct for the telecommunications inquires, in which case the Commission has over-quantified the benefits of price control of Transpower.
12. We note that many of the submissions (including Transpower's) raised similar concerns about the Commission's quantitative evaluation of the impact of price control on future investment.

Concluding remarks

13. TelstraClear would like to emphasise the importance of regulatory consistency. This does not mean that the Commission's approach should be exactly the same in all proceedings. Inevitably, the Commission's thinking will evolve and there will be industry/issue specific matters which means that differences are appropriate. It is important though that these differences and the reasons for these differences are transparent.
14. We trust the Commission finds TelstraClear's submission on these matters helpful and should the Commission wish to discuss any of the above points please contact Alistair Dixon on (04) 920-3098 or at alistair.dixon@team.telstraclear.co.nz.

Yours sincerely



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