

5 September 2014

## Open letter to parties regarding the FPP process

Dear Parties

### Process update

The purpose of this letter is to provide an update on the final pricing principle (FPP) process for the UCLL and UBA services. Before I do that I would like to take this opportunity to thank all parties for their engaging and helpful submissions to date. We appreciate that engaging with the FPP processes requires significant resource dedication from industry participants and we are grateful for the constructive way in which parties have contributed so far.

A number of concerns have been raised in submissions and correspondence regarding the process and timetable in which we are conducting the FPP price review determinations for the UCLL and UBA services. This letter responds to those concerns by sharing a number of aspects of our process to date, and our planning and proposed process to deliver the final price review determinations going forward.

As a number of interested parties have alluded to, a TSLRIC cost modelling exercise is a significant project for New Zealand's telecommunications industry and consumers.

We have prioritised the FPP price review determinations within our work programme. To ensure we have appropriate resources we have taken on a number of additional staff on a contract basis. This includes additional lawyers, economists, modellers, GIS staff, and a secondee from the Danish Business Authority (DBA) with experience building a TSLRIC model for telecommunication access services. Following a procurement process, we appointed French expert TSLRIC modelling consultants, TERA. We continue to work with a number of other expert consultants including Professor Ingo Vogelsang, Oxera and Associate Professor Martin Lally.

We are conducting a number of processes in the FPP price review determinations in parallel. These include:

- issuing extensive section 98 requests for data from which we may populate the TSLRIC models;
- sourcing of additional comprehensive third party data to enable mapping the unique features of NZ;
- confidentiality orders to allow parties access to confidential data we have collected; and
- consultation on the appropriate WACC.

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We have been greatly assisted by industry parties in the collection of data, understanding of wireless, copper and fibre networks, participation at workshops and their helpful submissions and cross submissions.

To assist parties, we have adopted a number of steps in our process:

- Sharing our external legal advice at the early stages of the development of our own thinking on a number of framework issues including on the selection of modern equivalent asset (14 March 2014) and on backdating prices (25 March 2014);
- Sharing economic and technical advice including on advice prepared by TERA on the effects of modelling choices (9 July 2014), and by Professor Ingo Vogelsang on the effects of the UCLL contribution to the UBA aggregate on competition for the long-term benefit of end-users in New Zealand telecommunications markets;
- Flying TERA to New Zealand to deliver a presentation to industry participants (9 April 2014), where they shared their experiences and knowledge on modelling TSLRIC methodology in other jurisdictions; and
- Hosting staff/industry workshops on 19 December 2013 and 28 March 2014 designed to assist parties with the development of their understanding of TSLRIC cost modelling issues. At these workshops, Commission staff shared their thinking, and parties discussed issues on a non-attributable “Chatham House rules” basis. Although Commissioners were not in attendance at these workshops, we have received positive feedback about their usefulness from a number of industry participants.

As we have previously signalled, we are targeting delivering draft price review determinations by 1 December 2014. In doing so, we were guided by the statutory direction to use our reasonable efforts to complete the review in that timeframe, and a desire to avoid protracted uncertainty for the industry over copper broadband pricing.

Although at this stage we have not elected to adopt as lengthy a process as advocated by some parties, we have planned the delivery of the FPP prices carefully, and have done so in a way which enables us to share our thinking as it develops and evolves. Different countries approach TSLRIC exercises differently. The length of the processes we have observed has varied, depending on the extent to which models include bottom-up as well as top-down elements, the extent of optimisation of networks modelled and the extent to which each country prioritises consultation with industry participants. One party pointed to the TSLRIC cost modelling exercise undertaken by the DBA to illustrate an appropriate process timeframe. When considering submissions, we were unconvinced that the DBA process was a useful a comparator, as it involved modelling three network technologies (copper, fibre and cable-tv), and involved additional consultation steps with the European Commission and other EU Member States. We also discovered that on another occasion, the DBA undertook a TSLRIC process in considerably less time than we have set out to do (around 12 months).

So far, we have conducted a number of consultation rounds throughout the UCLL and UBA FPP price review determination processes. In doing so (and as is often the case in other Commission projects) we have consulted more extensively than the statutory requirements in the Telecommunications Act. We have shared aspects of our framework as it has emerged and developed, and shared a more complete picture as some of our views have crystallised. We have shared and tested our thinking on fundamental modelling choices prior to beginning modelling. We have also consulted on a number of additional matters such as asset reuse – in fact, all of our thinking to date at the last consultation phase. Further consultations will be occurring over the coming months, including on



our proposed approach to service transaction charges. This approach to consultation has been adopted to assist parties with developing their understanding and engaging throughout the process, rather than working in isolation and sharing our fully developed thinking at draft determination stage. Incremental consultation has also been very helpful for us in terms of testing our thinking prior to commencing modelling. For example, stakeholder submissions on our July 2014 regulatory framework and modelling approach consultation paper have directly contributed to further refinement of that framework/approach.

Although we have not yet provided parties with a complete picture of all modelling choices by way of a Model Reference Paper (MRP), we intend to do so by 1 December 2014, together with additional documentation to assist their understanding, including the model specification, model user manual and our draft price review determination decision. Together, this suite of documentation will provide parties with the opportunity to understand and engage with the model and the reasoning for our draft decisions.

Following the release of the draft price review determinations, we will be working to ensure that parties have the opportunity to fully engage with the model, our reasoning and our process. We are planning to fly TERA consultants out from France to run a session with the industry to assist with understanding the model that TERA will have built by then. We are also planning an additional informal staff/industry workshop, and a more formal three day Conference attended by Commissioners. The Act provides for a maximum consultation period on the draft price review determinations of six weeks for submissions. However, the consultation period will be occurring over the Christmas and New Year period, which will be accounted for in submission timeframes.

We currently anticipate completing the final price review determinations by April 2015. However, as always, if new issues emerge during the draft price review determination consultation phase which require us to revisit and adjust our time frames, we will be flexible and responsive in our approach. Similarly, we accept that submissions may cause us to revisit a range of decisions in the draft determination, including modelling choices, and are open to doing so if necessary.

Once again I would like to thank parties for their constructive contributions to the process. We look forward to continuing to work with you at a staff and Commissioner level in pricing these broadband copper access services.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'S. Gale', with a stylized flourish at the end.

Dr Stephen Gale  
Telecommunications Commissioner