



# Cabinet Economic Growth and Infrastructure Committee

## Minute of Decision

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### Review of the Telecommunications Act 2001: Final Policy Decisions for Fixed Line Communications Services

Portfolio                      Communications

On 14 December 2016, the Cabinet Economic Growth and Infrastructure Committee (EGI):

#### Background

- 1        **noted** that in August 2015, EGI agreed to the release of a discussion document on the regulatory settings for communications markets after 2020 [EGI-15-MIN-0042];
- 2        **noted** that Ultra-Fast Broadband (UFB) pricing is currently controlled by contracts, which expire at the end of 2019, and that there is widespread support for the government to set in place a building blocks (BBM) pricing regime after that date;
- 3        **noted** that in March 2016, EGI made high level decisions in relation to the new pricing framework, including:
  - 3.1      to move to a utility-style regulatory regime with a building blocks (BBM) pricing methodology for UFB services from 1 January 2020;
  - 3.2      if BBM price control is implemented for Chorus' UFB services, that it also be implemented for its copper services;
  - 3.3      that these regulatory settings be established in the Telecommunications Act 2001 (the Act), rather than the Commerce Act 1986 (the Commerce Act);
  - 3.4      that the current obligation to unbundle the point-to-multipoint parts of the UFB network from 1 January 2020 be retained;
  - 3.5      that the government support a policy of maintaining price stability in the transition to a new regime;

[EGI-16-MIN-0040]
- 4        **noted** that in July 2016, EGI agreed to the release of an Options Paper seeking input on detailed implementation matters for the proposed pricing framework[EGI-16-MIN-0164];
- 5        **noted** that following analysis of the submissions received on the Options Paper and the receipt of external advice, the Minister for Communications and her officials have developed a detailed policy package to implement the pricing framework;

6 **noted** that:

- 6.1 the paper under EGI-16-SUB-0361 covers the pricing framework for fixed line services;
- 6.2 the Minister for Communications intends to separately bring proposals to EGI in early 2017 relating to mobile markets, and dealing with non-price issues such as dispute resolution, fault rectification and installation service levels;

7 **noted** that:

- 7.1 paragraphs 9 to 56 below relate to the fibre pricing framework;
- 7.2 the pricing framework for copper services is separately addressed in paragraphs 60 to 72 below;

8 **noted** that:

- 8.1 the decisions set out below are for the purposes of providing drafting instructions to the Parliamentary Counsel Office;
- 8.2 further amendments may be sought following public consultation;

### **Objectives and purpose**

- 9 **noted** that the objective of introducing a new pricing framework is to apply predictable and well-understood regulation to wholesale fixed broadband infrastructure that has inherent natural monopoly characteristics, for the long term benefit of end-users of communications services in New Zealand;
- 10 **agreed** that the purpose of the pricing framework be to promote the long-term benefit of end-users in markets for fixed line services by promoting outcomes that are consistent with outcomes produced in competitive markets, such that suppliers of regulated fixed line access services:
- 10.1 have incentives to innovate and to invest, including in replacement, upgraded, and new assets;
  - 10.2 have incentives to improve efficiency and provide services at a quality that reflects end-user demands;
  - 10.3 share with end-users the benefits of efficiency gains in the supply of the regulated goods or services, including through lower prices;
  - 10.4 are limited in their ability to extract excessive profits;

### **Pricing framework for fibre services**

- 11 **agreed** that the pricing framework for fibre comprise an initial regulatory period of three years (2020-2023), followed by repeating regulatory periods of a length to be determined by the Commerce Commission (within a range of 3-5 years);
- 12 **agreed** that the pricing framework for fibre will consist of two forms of regulation – information disclosure regulation and price-quality regulation;

- 13 **agreed** that all regulated suppliers (that is, Chorus, Ultra-fast Fibre, Northpower Fibre and Enable Networks, plus any new Local Fibre Companies created as part of the UFB extension programme) be subject to information disclosure regulation from 1 January 2020 onwards;
- 14 **agreed** that Chorus will additionally be subject to price-quality regulation from 1 January 2020 onwards;
- 15 **agreed** that the Act include:
- 15.1 a new Schedule that lists regulated suppliers and the forms of regulation they are subject to;
- 15.2 a process for introducing or removing suppliers from the Schedule, and for modifying the form of control of a regulated supplier listed in the Schedule;
- 16 **agreed** that there be an intervention test for the introduction of price-quality regulation for regulated suppliers that are subject only to information disclosure, which can be applied by the Commerce Commission at any time;
- 17 **agreed** that this intervention test be based on an equivalent intervention test for the introduction of price-quality regulation to consumer-owned electricity lines businesses in section 54H(2)(b) of the Commerce Act 1986;
- 18 **agreed** that:
- 18.1 the Commerce Commission regularly review whether competition has emerged for a service, market, asset or geographic location, and deregulate regulated suppliers accordingly;
- 18.2 this review is to be done prior to each regulatory period (except the first);

### Input methodologies

- 19 **noted** that the purpose of input methodologies is to promote certainty for suppliers and consumers in relation to the rules, requirements, and processes applying within the pricing framework;
- 20 **noted** that accordingly, the high-level rules, requirements and processes for the pricing framework will be set out in the Act, and the more detailed implementation aspects of these matters will be developed, consulted on and included in input methodologies;
- 21 **agreed** that the framework utilise input methodologies with the same features as for input methodologies in Part 4 of the Commerce Act, with additional requirements for the matters the input methodologies must cover, as required under the new framework (including quality and reliability requirements for the operation of networks);
- 22 **agreed** that the processes for developing, consulting on and implementing input methodologies be based on the approach in Subpart 3 of Part 4 of the Commerce Act;

**Regulated asset base**

- 23 **agreed** that the Act specify that each regulated fibre supplier, irrespective of the form of regulation applying to it, will have a ‘regulated asset base’ (RAB) with the following features:
- 23.1 each regulated supplier will have a single RAB containing fibre assets used to deliver the ‘fixed line access service’;
  - 23.2 at the outset of the regulatory framework, the Commerce Commission will develop an opening value for all fibre assets in the RAB;
- 24 **agreed** that the opening value of each regulated supplier’s RAB be determined by the Commerce Commission on the basis of the unrecovered historic costs incurred by the regulated supplier, but only to the extent that those costs were efficiently incurred;
- 25 **agreed** that in determining costs incurred for the RAB, the Commerce Commission must have regard to the government’s objectives of accelerating the widespread deployment of fibre-to-the-premise and encouraging end-user uptake, including by ensuring that:
- 25.1 efficient costs incurred as a direct result of meeting specific requirements in UFB or UFB extension programme contracts are included;
  - 25.2 efficient costs of ‘standard’ and ‘non-standard’ installations are included;
  - 25.3 the value of the opening RAB is increased by the financial losses efficiently incurred by suppliers prior to 2020 to the extent that those losses arose from meeting specific requirements under the UFB or UFB extension programme contracts (including the timeframes for rollout and the prices that can be charged);
- 26 **agreed** that:
- 26.1 there be a ‘major capital expenditure pre-approval’ mechanism where regulated suppliers will be able to seek pre-approval from the Commerce Commission for proposed capital investments that are significant (in value or nature) to be included in their RAB, in order to provide greater certainty of return on investment, based on the mechanism in place for Transpower in Part 4 of the Commerce Act;
  - 26.2 this will be developed in input methodologies by the Commerce Commission consistent with section 54S of the Commerce Act;
- 27 **agreed** that the RAB will then ‘roll forward’, adjusted for actual capital expenditure, economic depreciation, disposed or decommissioned assets, and indexed revaluations (where applicable) over time;

**Information disclosure regulation**

- 28 **noted** that the purpose of information disclosure regulation is to ensure that sufficient cost, revenue and other information about the performance of the regulated supplier is readily available to interested persons to assess whether the purpose of the new regime is being met (for example, that no monopoly profits are being earned);
- 29 **agreed** that information disclosure regulation be implemented in the framework with key parameters and requirements set in legislation, and detailed rules for implementation being developed by the Commerce Commission in input methodologies;

30 **agreed** that, under information disclosure, the Commerce Commission be required to publish summary reports containing an analysis of the information disclosed by each supplier subject to that form of regulation, including whether suppliers are making excess profits;

### **Price-quality regulation**

31 **noted** that paragraphs 32 to 55 below only apply to regulated suppliers that are subject to price-quality regulation;

32 **noted** that the purpose of price-quality regulation is to promote outcomes consistent with outcomes produced in competitive markets, in markets where there is little or no competition and little or no prospect of competition emerging, by constraining the overall revenues and the price and quality of services provided by regulated suppliers;

33 **noted** that a major feature of price-quality regulation is the fact that there are objective and measurable quality standards for the provision of services which are monitored and enforced by the Commission, and which are just as important as the price component, to incentivise ongoing quality improvements and to prevent regulated suppliers degrading quality in response to revenue constraints;

34 **agreed** that price-quality regulation be implemented in the framework, with key parameters and requirements set in legislation and detailed implementation rules being developed by the Commerce Commission in input methodologies;

35 **agreed** that price-quality regulation comprise:

35.1 an annual overall 'revenue cap' set for each regulated supplier;

35.2 a 'wash up' for the revenue cap, carried out prior to each new regulatory period (this is expanded on in paragraph 38 below);

35.3 a requirement to provide certain 'anchor' products on price, non-price, quality and reliability standards set by the Commission;

35.4 a requirement to provide all services on the network to certain minimum quality and reliability standards;

36 **agreed** that the Commerce Commission will determine an annual revenue cap for each regulated supplier (applying for the duration of the regulatory period) at the outset of each regulatory period;

37 **agreed** that the Commerce Commission be required to determine the annual revenue cap in a way that promotes price and revenue stability, by spreading any revenue increases over a regulatory period (or multiple periods) via altering the asset depreciation path, in order to "smooth" otherwise sharp changes in revenue affecting consumers, consistent with the criteria contained in section 53P(8) of the Commerce Act;

38 **agreed** that the revenue cap will be binding on the regulated supplier, and there will be a 'wash up' if it is exceeded or not achieved, as determined by the Commerce Commission in input methodologies:

38.1 if it is exceeded, then the revenue cap for the next regulatory period (or periods if necessary) will be reduced by a commensurate excess amount; or

38.2 if it is not achieved, then the revenue cap for the next regulatory period (or periods if necessary) will be increased by the commensurate shortfall amount;

39 **agreed** that:

39.1 regulated suppliers be required to provide certain anchor products to customer premises when requested to do so by a retail service provider (RSP), as long as the regulated supplier has its network connected to the customer premise, or it can reasonably be connected to the customer premise;

39.2 regulated suppliers will not be required to extend their networks only to provide an anchor product;

40 **agreed** that there will be two fibre anchor products in the initial regulatory period:

40.1 a 100/20Mbps UFB broadband product; and

40.2 a voice-only UFB product;

41 **agreed** that, in order to avoid the potential for sharp price changes for end-users, anchor product prices (from 1 January 2020) be set at 2019 levels for equivalent products, and be adjusted annually at the rate of inflation;

42 **agreed** that the Commerce Commission will thereafter be responsible for updating the specifications of the anchor product set, prior to each regulatory period, to ensure that it:

42.1 provides an upper limit on pricing for a product that is attractive to a large number of customers;

42.2 provides a price and quality 'anchor' for the other 'non-anchor' products provided by regulated suppliers;

43 **agreed** that the Commerce Commission will determine the price, non-price and quality terms for anchor products prior to each regulatory period (except the first), with criteria included in legislation for these decisions;

44 **agreed** that the Commerce Commission will determine minimum quality and reliability standards for the whole of the regulated supplier's network and services (applying to all types of services);

45 **agreed** that the Commerce Commission will set out these decisions in determinations in the same way as it does under Part 4 of the Commerce Act;

46 **agreed** that regulated suppliers will be free to determine the number, specification and pricing of all non-anchor products (except unbundled fibre services, as discussed below), subject to the revenue cap, the requirement for geographic averaging and minimum requirements as follows:

46.1 all services provided by suppliers must comply with minimum network quality and reliability requirements that will be set by the Commerce Commission;

46.2 suppliers must conduct industry consultation on price and non-price terms for non-anchor products, and commit to ongoing service development and RSP engagement;

46.3 suppliers must give at least six months' notice for changes to price or material non-price terms or withdrawal of non-anchor products;

- 47 **agreed** that, in order to enable the Commerce Commission to acquire the appropriate information for implementing regulation in accordance with the proposals in the paper under EGI-16-SUB-0361, the Commission be provided with an information gathering power consistent with that in Subpart 8 of Part 4 of the Commerce Act;
- 48 **noted** that regulated suppliers are already required under the open access deeds of undertaking (the Deeds) to provide an unbundled fibre service on the point-to-multipoint (GPON) parts of their networks from 2020, and on the point-to-point parts of their networks;
- 49 **agreed** that, in accordance with the Deeds:
- 49.1 regulated suppliers must provide the GPON unbundled fibre service from 1 January 2020;
  - 49.2 regulated suppliers must continue to provide the unbundled point-to-point fibre services;
  - 49.3 these will not be subject to regulated price caps initially, but the revenue from these services will be subject to the revenue cap;

### **Commerce Commission investigation into unbundling and/or change in form of control**

- 50 **noted** that it is important to provide a degree of flexibility within the pricing framework for fibre, and to maintain a credible regulatory threat of moving to a different form of control if necessary;
- 51 **agreed** to include a mechanism that, after 2023, enables the Commerce Commission to commence an investigation at any time after a certain overall threshold of fibre uptake has been achieved (for example, 65 percent) into:
- 51.1 whether the unbundled fibre services should become price-capped anchor products;
  - 51.2 whether anchor product prices should become purely cost-based;
  - 51.3 whether the 'form of control' should change from a revenue cap to 'price caps' (where all services provided by a supplier are subject to price caps set by the Commerce Commission);
- 52 **agreed** that the Commerce Commission will make a recommendation on any of the above matters, and that the final decision would be made by the Minister for Communications;
- 53 **agreed** that, in addition to the fibre uptake threshold that must be met, the Commerce Commission will need reasonable grounds to commence such an investigation, and that the process and criteria for the Commission to make any recommendation to the Minister for Communications will be set out in legislation;

### **Appeals and claw-backs**

- 54 **agreed** that the appeal and claw-back rights and obligations in the pricing framework for fibre be consistent with those in Part 4 of the Commerce Act:
- 54.1 input methodology determinations will be subject to merits review on the 'pure appeal' basis (but adopting a 'materially better' threshold);

- 54.2 consistent with section 91(1A) of the Commerce Act, reviews of final determinations on price-quality paths will be limited to matters not already reviewed under an input methodology review (therefore, this would be a ‘re-hearing’ approach for these determinations);
- 54.3 the Commerce Commission must apply claw-back when resetting price-quality paths if input methodologies change due to Court-ordered changes in an appeal process, and the amended input methodology would have resulted in a materially different price path (mirroring section 53ZB of the Commerce Act);
- 54.4 consistent with section 52D of the Commerce Act, if the Commerce Commission specifies a claw-back will occur, it must not place undue financial hardship on the supplier and any price shocks to end-users must be minimised;
- 55 **agreed** to include a provision making clear the respective roles and functions of the pricing frameworks for fibre and copper in the amended Act;

### Transitional arrangements

- 56 **agreed** that the Commerce Commission may ‘roll over’ regulated copper and contracted fibre prices at 31 December 2019 for up to 24 months if it is not ready to implement the pricing framework for fibre from 1 January 2020, with the prior written consent of the Minister for Communications;

### Open access deeds of undertaking

- 57 **agreed** that the Deeds (which continue to apply after 2020) be retained in their current form, and that they continue to apply to all fixed line services provided by regulated suppliers (irrespective of the form of regulation applying to each regulated supplier);
- 58 **agreed** that the prices of anchor products be exempt from ‘equivalence’ obligations under the Deeds;
- 59 **agreed** that, where a regulated supplier has more than one Deed applying to its business, these Deeds be consolidated into a single Deed without removing any of the obligations;

### Pricing regime for copper services

- 60 **noted** that:
- 60.1 on 30 March 2016, EGI agreed to include the copper network in the pricing framework for fibre [EGI-16-MIN-0040, paragraph 4];
- 60.2 following further submissions and analysis, the Minister for Communications now recommends a revised approach on the basis that it will produce better outcomes and greater certainty for consumers, investors and suppliers;
- 61 **agreed** to rescind the decision referred to in paragraph 60.1 above; and instead
- 62 **agreed** that, outside areas where UFB or other (non-UFB) fibre services are available, Chorus be required to continue providing the ‘unbundled bitstream access’ (UBA) wholesale copper broadband product as well as the ‘unbundled copper low frequency service’ (UCLFS) wholesale copper voice product (which supports the Telecommunications Service Obligation) on the same terms as it is required to do so on 31 December 2019;



- 63 **agreed** that the 2019 regulated prices for UBA and UCLFS, which have been set by the Commerce Commission, be ‘rolled over’ annually in nominal terms and continue to apply to those copper services that remain regulated from 1 January 2020;
- 64 **agreed** that, on 1 January 2020, copper services will be deregulated inside areas where UFB and other (non-UFB) fibre services are available;
- 65 **agreed** that, after 1 January 2020, there be a regular review mechanism whereby further deregulation of copper can take place as fibre is rolled out, and that deregulation of a particular area will be subject to the Minister for Communications being satisfied that fibre is sufficiently widely available in that area;
- 66 **agreed** that:
- 66.1 the pricing framework for copper services be reviewed by the Commerce Commission no later than 2023 to ensure it remains fit for purpose, with the Commission making recommendations whether to continue with the arrangements or modify them (for example, by re-regulating copper services if necessary);
- 66.2 final decisions will be made by the Minister for Communications;

### **Telecommunications Service Obligation**

- 67 **agreed** that the Telecommunications Service Obligation for Local Residential Telephone Service (TSO) be removed from Chorus and Spark inside areas with UFB or other (non-UFB) fibre from 1 January 2020;
- 68 **agreed** that the TSO obligations be retained on Chorus and Spark outside areas with UFB or other (non-UFB) fibre (to the outside TSO coverage footprint that currently applies);
- 69 **agreed** that the same mechanism as in paragraph 65 above be used for reviewing the removal of the TSO obligations from Chorus and Spark;

### **Copper withdrawal**

- 70 **noted** that:
- 70.1 where copper is deregulated, Chorus will have the option of withdrawing service and removing the copper network;
- 70.2 Chorus will be able to do this according to its own timeframes, but some minimum customer protection requirements will apply;
- 71 **agreed** to implement these customer protection requirements in a regulated code that applies to RSPs, as well as Chorus and Local Fibre Companies;
- 72 **agreed** that the code include certain requirements that must be met before Chorus is able to withdraw copper, as follows:
- 72.1 the availability of fibre services to the customer premise and the ability to install a UFB connection (if necessary) at no cost (except where the connection falls outside the ‘standard’ and ‘non-standard’ installation categories) to all affected premises in a reasonable time frame, so that end-users do not face a ‘gap’ without service when copper is withdrawn and before UFB is connected;
- 72.2 notice to be provided by Chorus, followed by a reasonable period of time to enable customers and RSPs to prepare before copper is withdrawn;

- 72.3 services currently able to be provided over copper must be available over fibre (except for legacy services such as facsimile);
- 72.4 information must be provided to customers about the change and the availability of services after the change (including in relation to the need for battery back-up on UFB services in the event of a power failure);
- 72.5 anchor products are available on the UFB network;

### Delegation to Ministers

- 73 **authorised** the Minister of Finance, the Minister for Economic Development and the Minister for Communications to make decisions on any further details or matters that arise in the implementation of the proposals in the paper under EGI-16-SUB-0361;

### Next steps

- 74 **invited** the Minister for Communications to issue drafting instructions to the Parliamentary Counsel Office to give effect to the above decisions, including any supporting amendments;
- 75 **noted** that:
  - 75.1 there will be further opportunity for detailed comment, and that the Ministry of Business, Innovation and Employment has advised that an exposure draft process would likely delay the introduction of legislation by more than three months, making a first reading unlikely in advance of the period of restraint that precedes a general election;
  - 75.2 this would introduce regulatory uncertainty and add to the risk that the new framework is not ready to operate by 2020;
- 76 **agreed** that public consultation be carried out on the scope of the BBM regime set out in paragraphs 11 to 14 and 62 to 66 above;
- 77 **noted** that the Minister for Communications may seek further decisions from EGI on any substantive policy proposals arising from consultation;
- 78 **noted** that the Minister for Communications will report to EGI in early 2017 reporting on the outcome of consultation and seeking agreement to introduce amending legislation.

Gerrard Carter  
Committee Secretary

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**Hard-copy distribution: (see over)**

**Present:**

Hon Gerry Brownlee  
Hon Steven Joyce (Chair)  
Hon Amy Adams  
Hon Simon Bridges  
Hon Dr Nick Smith (part of item)  
Hon Nathan Guy  
Hon Michael Woodhouse (part of item)  
Hon Todd McClay  
Hon Peseta Sam Lotu-Iiga  
Hon Maggie Barry  
Hon Craig Foss  
Hon Jo Goodhew  
Hon Nicky Wagner  
Hon Louise Upston  
Hon Paul Goldsmith

**Officials present from:**

Department of the Prime Minister and Cabinet  
Ministry of Business, Innovation and Employment  
Office of the Minister of Local Government  
Officials Committee for EGI

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Cabinet Economic Growth and Infrastructure Committee  
Deputy Chief Executive, Policy, DPMC  
Melleny Black, PAG, DPMC