

**Further work on the cost of capital input methodologies**

**Submission to Commerce Commission on**

**process update and invitation to provide evidence on the WACC percentile**

**5 May 2014**

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# Executive Summary

1. The Commission is seeking submissions providing:
   1. empirical or analytical evidence regarding the appropriate WACC percentile; and
   2. any additional considerations (supported by evidence) that differ between sectors and might affect the appropriate percentile.
2. The Commission is not seeking submissions on the extent to which a two-tier approach to the WACC may be appropriate, or any other features of the WACC IM. Accordingly Vector does not address those topics in this submission.
3. As a first point, Vector reiterates its serious concerns about the robustness of the process being run by the Commission and the lack of a sound basis for considering only one aspect of the WACC IM within such tight timeframes. The expert report prepared by Sapere Research Group (Sapere report) provided with this submission has been prepared within the time available. Sapere advise that, were more time available, it should be feasible to refine the analysis to help the Commission identify the degree of margin above the 75th percentile that would be necessary to achieve, on an expected basis, a welfare enhancing trade-off between the risk of understating WACC and the risk of overstating WACC.

# *Strong conceptual support for WACC above midpoint*

1. The starting point for the current consultation is that there is strong and broad-based support for setting the regulatory WACC above the midpoint estimate. This is primarily (but certainly not only) on the basis the costs to society of making incorrect decisions based on the WACC estimation are higher if WACC is underestimated than if it is overestimated.
2. The strong theoretical support for this proposition is evidenced by:
   1. previous expert evidence provided to the Commission, including from the Commission's own experts, and regulatory precedent from other jurisdictions; and
   2. the Commission's own reasons in adopting the 75th percentile.
3. The Sapere report accompanying this submission further considers the theoretical research and concludes that there is no doubt that asymmetric risk is real and important. Although there are limitations on the extent to which costs can be accurately quantified on a forward looking basis (especially within the timeframes of this consultation), it is clear that costs of under-estimating WACC will heavily outweigh the costs of over-estimating.
4. Given the above, setting the regulatory WACC above the midpoint estimate is consistent with the Part 4 purpose, and therefore an input methodology that does this is materially better at achieving the purpose than one that provides for a mid-point WACC (this position being reflected in the current WACC IM and the Commission's reasoning).

# *Evidence supports 75th percentile*

1. The Sapere report concludes that the available analytical evidence and inference from investment decisions would support the Commission adopting the 80th percentile or higher. In particular, the Sapere report:
   1. Finds that both theory and empirical research show that the estimate of WACC is subject to considerable error arising from errors in the parameter estimates and from inadequacies in the CAPM model (the Commission has recognised error in both but has not adjusted for error in the CAPM model; nor has it fully recognised the high degree of uncertainty in the CAPM based estimate of WACC arising from parameter error).
   2. Illustrates potential loss functions for linear, piecewise and LINEX estimates of the optimal percentile to minimise asymmetric costs.
   3. Concludes that a mixed loss function, where the loss is small for low over or underestimation but is exponential for significant underestimation, would appear to best model the loss from under or over estimation of WACC.
   4. Based on a review of the analytical and quantitative evidence, provides an order of magnitude estimate of the size of the potential welfare loss from a WACC that is set too high, and show that only a comparatively small amount of investment need be cancelled to produce a much larger economic loss were WACC understated by the same amount.
   5. Concludes that the available analytical evidence, and inferences from investment decisions, certainly support the Commission adopting at least the 75th percentile, if not higher, to account for the risks of parameter error. This evidence also suggests that the Commission should, in addition, allow for model error in its estimate of WACC.
2. These findings are also consistent with the Frontier report provided by Transpower and other expert reports we have seen.
3. Vector further submits that the Commission should not depart from its reasoning in support of its WACC IM determinations unless and until there is a sound evidential basis for doing so. This is where:
   1. the Part 4 framework, and the purpose of IMs in particular, implicitly require that the IMs, once determined, are consistently applied and changed only where there is a sound evidential basis; and
   2. regulatory commitment and consistency (being well accepted regulatory best practice principles) are critical to confidence in a regime and incentives to invest.
4. Currently there is no evidence to support the Commission adopting a different approach:
   1. While the High Court questioned the basis for the 75th percentile, the Court was clear that these comments were made without any evidential basis.
   2. The only expert report to question setting the regulatory WACC above the midpoint estimate in this context was provided by NZIER on behalf of MEUG in March 2014 (despite this issue being "live" over the last 10 years). However, NZIER does not suggest that the conceptual position set out above is incorrect, but only that there is a lack of empirical evidence to justify applying a WACC above the midpoint estimate.
   3. Vector does not agree that the Northington report is evidence that the 75th percentile WACC is higher than needed and refers to an expert report by PwC (PwC report) provided with this submission to support that position.

# Introduction

1. The Commerce Commission (Commission) issued a notice of intention to undertake further work on the cost of capital input methodologies (WACC IMs) on 31 March 2014.
2. This submission is in response to the Commission's process update and invitation to provide evidence on the WACC percentile, also issued on 31 March 2014.
3. Attached to this submission are expert reports from Sapere *Setting the WACC percentile for Vector’s price-quality path,* dated 4 May 2014, and from PwC *Rationale for transaction premiums to RAB value,* dated 28 March 2014.
4. The Commission in its invitation is seeking submissions providing:
   1. empirical or analytical evidence regarding the appropriate WACC percentile; and
   2. any additional considerations (supported by evidence) that differ between sectors and might affect the appropriate percentile.
5. At the outset, Vector notes that:
   1. The short form and limited consultation process is insufficient to enable robust and comprehensive analysis of potential new methods to determine the WACC estimate (i.e. “percentile”). The evidence provided by Vector in response to the Commission's invitation is subject to this caveat.
   2. As the Commission is not seeking submissions on the extent to which a two-tier approach to the WACC may be appropriate, or any other features of the WACC IMs, those topics are not addressed in this submission or the accompanying reports. If, during this consultation process, the Commission takes account of the two-tier approach (or other aspects of the WACC IMs) in its reasoning, we would reasonably expect a full and further opportunity to provide evidence on the issues in question.
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# Strong conceptual support for WACC above midpoint

1. The question posed by the Commission in this consultation round is narrow, relating only to evidence regarding the appropriate WACC percentile. However, it is important to place that question in context. That context is that there is strong conceptual support for the proposition that the risks in relation to regulatory error in setting the WACC are asymmetric, such that the regulatory WACC should be set above the midpoint estimate. Indeed, this is the position that has been adopted by the Commission in the current WACC IMs. We set out key aspects of this support below.
2. First, the Commission's own economic advisers have consistently supported setting the regulatory WACC above the midpoint estimate, both prior to the inception of Part 4 and in the context of consultation on the WACC IMs. In the control inquiries under the previous regulatory regime, Dr Lally (for the Commission) expressly endorsed a regulatory WACC above the midpoint because of the asymmetric risks of regulatory error.[[1]](#footnote-1) In consultation on the WACC IMs, the Commission's advisors again recommended this approach:[[2]](#footnote-2)

155. As a general principle, the Commission considers that the costs of setting allowed returns too low outweigh the costs of setting them too high. Therefore, the Commission generally chooses WACC values either equal to, or greater than, the midpoint of the estimated range. Professors Myers and Franks agree with this principle.

156. Dr Lally's view is that the Commission needs to specify a WACC value that is strictly greater than the midpoint of the range, not simply equal to it. Several submitters (ABN AMRO; JB Were; LECG; NERA; PWC; Transpower; Vodafone) have urged the Commission to consistently select values from the upper end of the estimated WACC range.

1. Second, the proposition was also endorsed by a significant number of experts on behalf of submitters in the WACC IMs consultation process.[[3]](#footnote-3) Notably, although MEUG consistently opposed the use of a regulatory WACC above the midpoint estimate, it did not provide any expert evidence in support of its position.
2. Third, the Commission has itself adopted the approach that the regulatory WACC for Electricity Distribution Services (EDSs), Gas Pipeline Services (GPSs) and Transpower should be set above the midpoint estimate. As set out in the Final Reasons Paper:[[4]](#footnote-4)

The reason for the Commission adopting a cost of capital estimate that is above the mid-point for default/customised price-quality regulation, is that it considers the social costs associated with underestimation of the cost of capital in a regulatory setting involving constraining pricing to end users (as opposed to information disclosure applications and situations involving competition among suppliers), are likely to outweigh the short-term costs of overestimation (i.e. if the cost of capital is set too low, the incentives for suppliers to undertake efficient investments will be reduced, which would be inconsistent with the long-term benefit of consumers). That is, the Commission is acknowledging that where there is potentially a trade-off between dynamic efficiency (i.e. incentives to invest) and static allocative efficiency (i.e. higher short-term pricing), the Commission will always favour outcomes that promote dynamic efficiency. The reason is that dynamic efficiency promotes investment over time and ensures the longer term supply of the service, which thereby promotes the long-term benefit of consumers (consistent with outcomes in workably competitive markets).

1. This approach is consistent with that of overseas regulators, who also often make adjustments to account for the asymmetric cost of WACC estimation error, although they use a variety of methods to do so (**Appendix 1** sets out relevant precedent in this regard, as previously provided by Vector in this consultation process).
2. The Sapere report that accompanies this submission sets out the grounds for the conclusion that the risks in relation to regulatory error in setting the WACC are asymmetric, such that the regulatory WACC should be set well above the midpoint estimate. In summary, Sapere’s report finds that, given the relatively inelastic demand for electricity and gas distribution services, the deadweight losses associated with prices that are inefficiently high are relatively small, whereas the welfare losses associated with the deferred or cancelled investment in network assets that would result if the regulatory WACC was set too low are significant.[[5]](#footnote-5)
3. In summary, then, the starting point for the current consultation is that there is strong and broad-based support for setting the regulatory WACC well above the midpoint estimate. Further, and critically, the Commission's reasoning in support of the 75th percentile reflects this strong support.[[6]](#footnote-6)

# Allowance for asymmetric costs consistent with Part 4 Purpose

1. As explained above, a WACC estimate above the mid-point increases the likelihood that the true WACC is at least achieved and that, accordingly, there are sufficient incentives for efficient and necessary investment to occur. On the other hand, a lower WACC estimate increases the risk that the true WACC will not be achieved. As the Commission set out in its Final Reasons Paper, "if the cost of capital is set too low, the incentives for suppliers to undertake efficient investments will be reduced, which would be inconsistent with the long-term benefit of consumers" (see paragraph 21 above).
2. As also noted above there is a general consensus at a conceptual level that the costs of regulatory error in setting the regulatory WACC are asymmetric, such that consumer welfare will be maximised by setting the regulatory WACC above the midpoint estimate. Accordingly, in the context of the Part 4 regime, setting the regulatory WACC above the midpoint estimate (in order to mitigate against the risk that the true WACC is not achieved) is necessary in order to promote the Part 4 purpose.
3. The new Part 4 sought to ensure the Commission placed increased and express focus on incentives to invest.[[7]](#footnote-7) This is reflected in the wording of section 52A(1), where:
   1. The ultimate aim of Part 4 is to "promote the long-term benefit of consumers" in the relevant markets.
   2. The means for achieving this goal is "by promoting outcomes that are consistent with outcomes produced in [workably] competitive markets" such that (a) to (d) are met.[[8]](#footnote-8)
   3. To the extent that a balance needs to be struck between (a) to (d), the long-term benefit of consumers is the arbitrating principle as this is the ultimate aim of Part 4.
4. In economic terms, the long-term benefit of consumers will be achieved if the economic welfare of consumers (consumer surplus), over the long-term, is maximised. Investment is a very important contributor to this consumer welfare in the long-term. This economic proposition is not disputed by the Commission (at the level of principle), having stated that:[[9]](#footnote-9)

… innovation and efficient investment over time can deliver significant long-term benefits to end-users, and the adverse consequences of deterring or delaying such investments may be substantial.

1. Where there is a trade-off between incentives to invest and higher short-term prices, the Commission's position is that it will always favour the former on the basis that this best promotes the long-term benefit of consumers (consistent with the Part 4 purpose).[[10]](#footnote-10)
2. In summary, in Vector's submission, setting the regulatory WACC above the midpoint estimate is consistent with the Part 4 purpose, and therefore an input methodology that does this is materially better at achieving the purpose than one that provides for a mid-point WACC. The amount of the required increment is a matter of quantitative assessment to the extent such an assessment is possible, bearing in mind that estimating WACC ultimately remains an imprecise exercise.

# *Merits review judgment*

1. The above analysis is generally consistent with the High Court's approach in the merits review judgment to the Part 4 purpose statement. However, in its *obiter* comments in relation to the 75th percentile issue, the Court stated that the Commission's choice of the 75th percentile estimate was "clearly at odds" with s 52A(1)(d).[[11]](#footnote-11) Vector respectfully questions whether this comment is correct in law: the Court appears to be reading the s 52A(1)(d) purpose of "limiting" the ability of regulated suppliers to extract excessive profits as a purpose of "eliminating" such profits. This point was expressly made by suppliers,[[12]](#footnote-12) but not addressed by the Court. Further, the Court does not appear to consider that, even at the 75th percentile, there is the possibility that the WACC does not allow a normal return (and therefore should not be characterised as locking in an expectation of excessive returns)*.* In any case (and consistent with theanalysis above), the Court went on to ask whether the possibility of "excessive profits" was justified by a fear of failing to promote incentives to innovate and invest,[[13]](#footnote-13) and held that the answer to that question was to be decided by reference to what best promotes the long-term benefit of consumers.[[14]](#footnote-14)

# Evidence supports 75th percentile

1. Thus far, the Commission has exercised its judgement, having regard to the relevant factors, to set the WACC for price/quality control purposes at an estimate of the 75thpercentile rather than at the midpoint estimate. The question raised by the Court was whether further evidence was needed and / or whether it was possible to obtain further evidence to justify the choice of percentile.
2. As set out in the Sapere report, quantitative economic analysis strongly supports setting the regulatory WACC at or above the Commission's 75th percentile estimate. In summary:
   1. The Commission's 75th percentile estimate is not an unbiased estimate of the 75th percentile of the sampling distribution, because the Commission has not taken into account any potential sources of error other than parameter error, nor has it recognised the significant degree of uncertainty in the CAPM based estimate of WACC resulting from parameter error.[[15]](#footnote-15)
   2. Hence, the Commission cannot be sure that an estimate of WACC made according to its approach (without a margin) achieves for investors an expectation of a normal return.[[16]](#footnote-16)
   3. Economic theory seems unambiguous; the economic loss to society of making incorrect decisions based on the WACC estimate are higher if WACC is under estimated than if it is over estimated.[[17]](#footnote-17)
   4. A mixed loss function, where the loss is small for low over or underestimation but is exponential for significant underestimation, would appear to best model the loss from under or over estimation of WACC.[[18]](#footnote-18)
   5. Sapere provides an order of magnitude estimate of the size of the potential welfare loss from a WACC that is set too low and a WACC that is set too high. They show that only a comparatively small amount of investment need be cancelled to produce a much larger economic loss were WACC understated by the same amount.[[19]](#footnote-19)
   6. Sapere concludes that the available analytical evidence, and inferences from investment decisions, certainly support the Commission adopting at least the 75th percentile, if not higher, to account for the risks of parameter error. This evidence also suggests that the Commission should, in addition, allow for model error in its estimate of WACC.
3. Vector notes that a similar conclusion has been reached by Frontier for Transpower and in other expert reports we have seen.[[20]](#footnote-20)
4. Sapere emphasises that its findings reflect the work that it was possible to complete to a reasonable level of rigour within the timeframes set by the Commission. Were more time available, Sapere advise that it should be feasible to refine their analysis to help the Commission identify the degree of margin above the 75th percentile that would be necessary to achieve, on an expected basis, a welfare enhancing trade-off between the risk of understating WACC and the risk of overstating WACC. In our view the Commission should review its process for this IM review and make further time available for experts to further develop their analysis and peer review each others’ work.
5. Finally, Vector notes that the Commission has previously suggested that certain observations of Northington Partners regarding the valuation of Transpower and the recent acquisition of a 42% equity stake in Powerco imply the 75th percentile WACC is higher than needed to promote efficient investment. As foreshadowed in its submission dated 13 March 2014, Vector has commissioned an expert review by PwC of the Northington analysis, which is attached to this report. Key conclusions of PwC include:
   1. It is not clear why Northington has applied different parameters in their calculation of WACC, compared to the parameters adopted by the Commission. For example, the risk free rate adopted by Northington is 75bps lower than that used in RCP2 (which is the period over which most of the cash flows are earned). One of the direct impacts of this approach is the differential that arises between WACC and regulated returns.
   2. Their analysis shows six reasons why a premium to the regulatory asset base value might be paid that are unrelated to an investor adopting a lower cost of capital. Accordingly, in nearly all cases where an investor pays a premium to the regulatory asset base value, this is NOT because that investor has adopted a lower cost of capital.
6. In short, PwC disagrees that the Northington report is evidence that the 75th percentile WACC is higher than needed. Evidence is required to justify a change in approach.
7. Vector further submits that the Commission should not depart from its reasoning in support of its WACC IM determinations unless and until there is a sound evidential basis for doing so. As explained further below, this is where:
   1. the Part 4 framework, and the purpose of IMs in particular, implicitly require that the IMs, once determined, are consistently applied and changed only where there is a sound evidential basis; and
   2. regulatory commitment and consistency (being well accepted regulatory best practice principles) are critical to confidence in the Part 4 regime and incentives to invest.

# *Part 4 framework / regulatory best practice*

1. In relation to the legislative framework, Part 4 does not envisage constant or arbitrary change to the IMs (or to the reasoning adopted in the IMs). This is where:
   1. Critically, changing regulatory approaches to the IMs without good reason is contrary to the overarching certainty objective in section 52R and the Part 4 purpose (where certainty is considered a pre-requisite to incentives to invest).
   2. The Commission is required to determine the IMs to be applied at the commencement of the regime, which then must be published and are subject to merits review (and possibly further), appeal, the IMs thus being clearly intended to have a long-lasting and precedential effect; [[21]](#footnote-21) and
   3. The Commission is required only to "review" the IMs within seven years.[[22]](#footnote-22)
2. The Part 4 regime also implicitly requires adherence to regulatory best practice principles. This is because the regulator's behaviour has a direct impact on regulatory certainty, and therefore on incentives to invest and the long-term benefit of consumers (the central purpose of Part 4). It is axiomatic that commitment and consistency are key principles of regulatory best practice and are critical to confidence in the regime and incentives to invest.[[23]](#footnote-23)

# *Evidence is required that its reasoning was wrong before the Commission abandons its reasons for adopting the 75th percentile*

1. The percentile provided for in the current WACC IMs, and the Commission's reasons for adopting this percentile, must necessarily be treated as the appropriate starting point for the current consultation. It would be contrary to the Part 4 framework and poor regulatory practice for the Commission to radically change its reasoning and abandon its approach without sound basis.
2. In our view, it is particularly inappropriate for the Commission to depart from its decision on the WACC IMs in circumstances where the process that led to the IMs in question was lengthy, considered, and made heavy use of expert conferences and evidence.
3. The Commission process update paper, and earlier consultation paper, gives the impression that the Commission is distancing itself from its reasoning in support of the current IMs and is in effect starting afresh, before any clear contrary evidence has been provided or considered.[[24]](#footnote-24) This raises concerns about the Commission's commitment to its previous approaches across all IMs, not just the 75th percentile. Vector emphasises here that the Court itself observed that its *obiter* comments - ostensibly the Commission's reasons for initiating the current consultation - were without evidential basis.[[25]](#footnote-25)
4. In relation to the appropriate starting point, the Commission's reasoning in support of the 75th percentile is outlined above. This is the reasoning and position that should be maintained in the absence of factual evidence that a lower percentile is required. Vector notes that no evidence has been provided which would justify the Commission abandoning its existing regulatory position. That is, the Commission should not now start from a position that the 50th percentile is the appropriate percentile unless evidence is provided otherwise. Instead the Commission should start from a position that the 75th percentile is appropriate unless robust evidence is provided to demonstrate that a different percentile (higher or lower) is more appropriate.

# Process insufficiently robust

1. Finally, Vector reiterates its concerns about the robustness of the current process being run by the Commission. This is a position that has been raised by a number of submitters, including MDL (who the Commission relies on in support of its truncated approach). These concerns have also been outlined in a recent letter from the Electricity Networks Association to the Commission sent on 2 April 2014.
2. As stated in Vector's 13 March 2014 submission on this consultation, in addition to creating uncertainty, the Commission's proposed "short-form" consultation risks a poor quality decision because:
   1. considering the WACC percentile in isolation ignores critical interdependencies with the other elements of the WACC calculation and the broader regulatory and market environment; and
   2. even if the appropriate percentile is considered in isolation from other aspects of the WACC, the time frame is too short to allow for a robust process where all relevant evidence can be fully considered.
3. With regards to the process and time frames set out for the current consultation, our particular concerns include the fact that:
   1. there is no opportunity for experts to comment on other parties' expert reports and the Commission has not even provided time for cross-submissions to be provided on the expert evidence submitted in this round of consultation;
   2. there is no indication whether the Commission will release reports from its own experts, and whether there will be an opportunity to submit on those reports;
   3. there is no time allowed for a workshop conference, and no discussion of why one has not been provided for (Vector considers a conference to be critical given it provides an opportunity for the Commission to question and hear from experts);
   4. the timeframes set are unreasonably short, and will result in extreme workloads given the complexity and materiality of the subject matter and the need to instruct experts and manage availability constraints (especially given the DPP reset consultation is progressing in parallel); and
   5. as noted above, the Commission is not allowing for full consideration of inter-linkages between WACC parameters and other IMs to ensure that asymmetric risk and model error are properly accounted for within the WACC IMs and the regime as a whole.

# Conclusion

1. Despite submitter's best efforts, it is apparent that further time is required to refine the expert analysis to inform a decision on the appropriate WACC percentile.
2. In light of our ongoing and increasing concerns about the adequacy of the consultation process, and the lack of any sound justification for the compressed time frames, Vector urges the Commission to extend the current timetable and the scope of the matters being considered.

1. See, for example, Martin Lally *The Weighted Average Cost of Capital for Electricity Lines Businesses* (8 September 2005) and *The Weighted Average Cost of Capital for Gas Pipeline Businesses* (28 October 2008). [↑](#footnote-ref-1)
2. Julian Franks, Martin Lally and Stewart Myers *Recommendations to the New Zealand Commerce Commission on an Appropriate Cost of Capital Methodology* (18 December 2008) at [155]–[157]. [↑](#footnote-ref-2)
3. See, for example, Synergies Economic Consulting *Selected issues arising from Commerce Commission’s Input Methodologies Discussion Paper* (August 2009) at VII; PwC *Revised Draft Guidelines – Submission to Commerce Commission on behalf of Powerco* (August 2009) at 7-8; Synergies Economic Consulting *WACC Review: Final– Report Prepared for Vector* (31 August 2009) at 15 and section 8; Uniservices *Comments on the Commerce Commission‘s Approach to estimate Cost of Capital (report prepared for NZAA)* (2 December 2009); Uniservices *Comments on Air New Zealand‘s and BARNZ‘s Submissions to the Commerce Commission‘s Approach to estimate the Cost of Capital in its Input Methodologies Draft Reasons Paper (report prepared for NZAA)* (3 August 2010); Tony van Zijl (LECG) *Response to Commerce Commission’s Draft Cost of Capital Input Methodology (Prepared for ENA)* (13 August 2010) at [17]-[24]; KPMG *Cross Submission to Commerce Commission on Input Methodologies Gas Pipeline Services: Draft Reasons Paper (prepared for Maui Development Ltd)* (13 August 2010). [↑](#footnote-ref-3)
4. Commerce Commission, *Input Methodologies (Electricity Distribution and Gas Pipeline Services)* Reasons *Paper,* 22 December 2010 (Final Reasons Paper), at [H1.31]. [↑](#footnote-ref-4)
5. Sapere Report, sections 5.2 and 5.3. [↑](#footnote-ref-5)
6. See paragraphs 38-40 below, which discuss the importance of regulatory commitment - that a regulator should not abandon reasoning and approaches without a sound evidential basis. [↑](#footnote-ref-6)
7. See for example, Cabinet Economic Development Committee, *Review of Parts 4 and 4A of the Commerce Act*, 22 January 2008, para 7; Dalziel, L. and Parker, D., "Bill gives better incentives for infrastructure investment", 13 March 2008. [↑](#footnote-ref-7)
8. Competition is defined in the Act as workable or effective competition: see section 3(1). [↑](#footnote-ref-8)
9. Commerce Commission, *A Guide for Regulatory Decision Making by the Commerce Commission in the Telecommunications Sector - Discussion Paper* (31 July 2009), p 28. [↑](#footnote-ref-9)
10. Final Reasons Paper, at [H1.31]. [↑](#footnote-ref-10)
11. *Wellington International Airport Limited v Commerce Commission* [2013] NZHC 3289 (MR Judgment), at [1460] - [1461]. [↑](#footnote-ref-11)
12. MR Judgment, at [264]. [↑](#footnote-ref-12)
13. MR Judgment, at [1460] - [1461]. [↑](#footnote-ref-13)
14. MR Judgment, at [1461]. [↑](#footnote-ref-14)
15. Sapere report, section 2.2. [↑](#footnote-ref-15)
16. Sapere report, sections 2.4 and 3.3. [↑](#footnote-ref-16)
17. Sapere report, section 4. [↑](#footnote-ref-17)
18. Sapere report, section 4.4. [↑](#footnote-ref-18)
19. Sapere report, section 5. [↑](#footnote-ref-19)
20. Frontier Economics, *Evidence in support of setting allowed rates of return above the midpoint of the WACC range - A report prepared for Transpower New Zealand Ltd* (13 March 2014), pp iii, iv, 21 - 24. [↑](#footnote-ref-20)
21. Section 52Z. [↑](#footnote-ref-21)
22. Section 52Y. [↑](#footnote-ref-22)
23. The importance of regulatory commitment has been recognised previously by the Commission, see for example the Final Reasons Paper at para 4.3.4 where the Commission notes that "monitoring or setting prices on a materially different basis to that used in the past would be likely to damage the confidence that suppliers and/or consumers have in the arrangements put in place under Part 4. [↑](#footnote-ref-23)
24. For example, the Commission refers to gathering further evidence in order to "form a view" on the appropriate percentile (see Commerce Commission, *Notice of intention to undertake further work on the cost of capital input methodologies*, 31 March 2014 at para 18. [↑](#footnote-ref-24)
25. See, for example, MR Judgment at [1482], where the Court stated that its 'in principle' objections to the Commission's use of the 75th percentile suffered from the same lack of empirical support as the Commission's approach. In addition, the Court was not satisfied MEUG's proposed amendments to the WACC IM regarding the 75th percentile would be materially better at meeting the purposes laid out in sections 52A and 52R (at [1483]). [↑](#footnote-ref-25)