Regulatory Impact Statement

LEVY REGULATIONS TO FUND THE IMPLEMENTATION OF PART 4 OF THE COMMERCE ACT 1986

EXECUTIVE SUMMARY

The Commerce Act has been amended to put in place a revised regulatory regime for electricity lines businesses (including Transpower), gas pipeline businesses and major international airports. New levy regulations are required in order to recover the Commerce Commission's costs of developing and administering the regime.

The Commerce Commission's costs for implementing the new Part 4 can be divided into (i) the cost of developing Input Methodologies (IM's) for all regulated sectors and, (ii) the costs of administering regulatory requirements for each regulated sector. The levy regulations are intended to set out how the Commission's costs under Part 4 are to be recovered and in particular how the costs are to be allocated between regulated parties. The cost allocation methodology should be fair, consistent and straightforward to administer.

On the basis of these principles, the preferred approach for cost allocation is relative share of fixed asset valuation. This would allocate the costs of administering each sector's specific regulatory regime between participants in that sector based on each company's relative asset valuation (using the valuation methodology of the Commission). The costs of developing IM's for the regulated sectors would be allocated to businesses based on each business' asset valuation relative to the total asset valuation of the three regulated sectors combined.

ADEQUACY STATEMENT

The Ministry of Economic Development (MED) confirms that the Code of Good Regulatory Practice and the regulatory impact analysis requirements, including the consultation RIA requirements, have been complied with. Adequate consultation has been undertaken.

STATUS QUO AND PROBLEM

The Commerce Act was amended in October 2008 to provide for a revised regulatory regime for electricity lines (including Transpower) and gas pipelines businesses, and a new regulatory regime for major international airports under Part 4. This regime replaces the old Part 4, 4A and sections of Part 5 of the Act. There are existing levy regulations that provide for the collection of the Commission's costs relating to the regulation (under the Commerce Act) of electricity lines businesses and of Powerco's and Vector's Auckland distribution gas pipelines businesses. The electricity levy regulations allocate levies on the basis of share of total fixed asset valuation. The levy regulations for Powerco and Vector allocate levies based on the parties paying an equal share of the Commission's costs.

If the existing electricity and gas sector levy regulations are not amended or replaced, and if new levy regulations for major international airports are not made, the costs incurred by the Commission in implementing and administering the new regime will not be able to be recovered from regulated businesses.

OBJECTIVES

The objectives of the levy regulations are to recover the Commission's costs of implementing and administering the regulatory regime for electricity lines businesses, gas pipeline businesses and major international airports. In recovering the Commission's costs from regulated parties, the levy regulations should allocate the costs between businesses using a consistent and fair methodology that is straightforward to administer.

ALTERNATIVE OPTIONS

An alternative option is for the Crown to fund the costs of Part 4 regulation incurred by the Commission. The costs would therefore be met through general taxation.

This option is not preferred as the costs of the regime (by way of taxation) would not be borne by those who are the direct beneficiaries of the regulation. There are also alternative options for the basis of levy allocation between businesses.

Option 1: Relative share of end-customers

This option would allocate the cost of administering each sector's regulatory regime to its participants based on each company's proportion of end-customers in that sector. It would allocate the Commission's costs for developing IM's between all businesses in all sectors based on each company's relative share of end-customers.

The advantage of this option is its administrative simplicity which would mean it would be cost-effective. The relative shares of end-customers are easily obtainable figures.

The main disadvantage of this option is that it does not take into account the different characteristics and thus costs of customers for different businesses. For example, in the airport sector, the relative share of passengers would not distinguish between international and domestic passengers, or long haul and short haul passengers. These different types of passengers will generate different levels of revenue and require different levels of cost. Within the electricity sector, Transpower does not supply end-customers. Overall, using end-customers is likely to be relatively inequitable as a basis for allocating IM costs to businesses across sectors as the measurement has no relation to ability to pay.

Option 2: Relative share of revenues

This option would allocate the Commission's costs of administering each sector's regulatory regime to its participants based on each company's proportion of revenue in that sector. It would allocate the cost for developing IM's between all businesses in all sectors based on each company's relative share of revenue.

The advantages of this option is that it would be relatively simple to administer so could be cost-effective. It would also be based on existing pricing practices and thus, it may be argued, be more representative, for example, of regulated airports' ability to pay.

The disadvantage of this option is that the relative share of revenues is likely to fluctuate more than the value of fixed assets. This would provide less regulatory certainty to businesses upfront in relation to the proportion of the levy parties will be allocated.

Option 3: A combination of a flat fee and a variable fee

This option would involve regulated parties paying an amount that would comprise a flat fee (based on fixed or common costs that are incurred from implementing and administering the regulation), and a variable fee which could be based on relative shares of fixed asset valuations.

The advantage of this option is that it could be more reflective of the costs incurred in regulating individual regulated businesses.

The disadvantage of this option is that consumers on small networks would pay relatively more than other consumers (depending on the size of the flat fee) and it would add administrative complexity and costs. On balance, the marginal benefits of this approach would not outweigh the costs of developing and applying a more complex allocation methodology.

None of these options are preferred as a basis for allocation of the levy.

PREFERRED OPTION

The preferred option is the recovery of costs from electricity lines businesses, gas pipeline businesses and the major international airports through levy regulations.

We consider that a levy on industry will better ensure that costs are more accurately passed on to those who benefit; the consumers of the service. This is the most appropriate option because consumers themselves will be the main beneficiaries of the regulatory regime, so there is a stronger case for costs to be recovered from them rather than from taxpayers.

The preferred basis of levy allocation for all three sectors is relative share of fixed asset valuation. This means businesses pay a proportion of the costs of regulation relative to the size of their business.

On balance, and relative to alternative options, the share of fixed asset valuation was the preferred option for its consistency across sectors and between businesses, fairness, and administrative simplicity.

This option was developed taking into account the Treasury's Guidelines for Setting Charges in the Public Sector (2002). The Audit Office Guidelines on Charging Fees for Public Sector Goods and Services (2008) do not apply to levies (refer paragraph 1.10 of the guidelines).

IMPLEMENTATION AND REVIEW

Electricity lines businesses, gas pipeline businesses and major international airports are aware that levy regulations are being developed, and will be notified of the recommended levy design and when the regulations are to be promulgated.

CONSULTATION

Consultation on the decision to recover costs through a levy on regulated parties was undertaken through consultation on the Commerce Amendment Bill 2008, as the levy regulation making powers were part of this Bill.

In accordance with 53ZE (4) of the Commerce Act 1986, regulated parties were consulted on a proposed levy design. A discussion paper was posted on the Ministry of Economic Development website for public consultation and directly sent to electricity lines businesses, gas pipeline businesses and major international airports for comment. The views of submitters have been taken into account in the proposed levy design.