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Dear Mr Motherwell

Assessment of expenditure forecasts

1. In order to inform the Commonwealth's position regarding the drafting of the electricity distribution revenue rules you have asked for advice about the ability of the Australian Energy Regulator (AER) to reject proposals of operating and capital expenditure under:
 - a. the Australian Energy Market Commission's (AEMC) proposed electricity transmission revenue rules in the Draft National Electricity Amendment (Economic Regulation of Transmission Services) Rule 2006 (the proposed Rule); and
 - b. an alternative formulation.

You seek clarification on the key points below.

QUESTIONS AND SHORT ANSWERS

2. Your questions and our short answers are as follows:
 - Q.1. *Does the decision making model in the AEMC's proposed Rule represent a 'consider-decide' or 'propose-respond' decision making model for capital and operating expenditure?*
 - A.1. The proposed Rule is a limited 'propose-respond' model. The proposed Rule allows the service provider to submit a proposed estimate of capital and operating expenditure which the AER must assess as to whether or not the total (or a total revised after a draft decision) is a reasonable estimate. If the total is determined to be a reasonable estimate, taking into account the twelve factors listed in the proposed Rule, it must be accepted by the AER. If the total is determined not to be a reasonable estimate, the AER may replace it with what it considers to be a reasonable estimate. This makes it a limited 'propose-respond' model as understood by the Expert Panel, as opposed to a 'consider-decide' model where the AER would simply determine expenditure taking into account whatever factors the Rule requires.

- Q.2 *When given a total estimate of operating or capital expenditure with information that meets the submission guidelines, does the AER need to make a determination of whether that total is a reasonable estimate?*
- A.2. Yes. The drafting of the proposed Rule, and in particular the procedural provisions in proposed Rule 6A.14, makes it clear that the key task of the AER is to assess whether the proposed total is a reasonable estimate or is not a reasonable estimate. Essentially, the AER cannot substitute a new total unless it reaches a decision that the proposed total is not reasonable; in summary terms, this requires a decision that the proposed total is unreasonable before the AER can substitute a new decision (see proposed Rule 6A.12.1(b), 6A.13.1(b), 6A.14.1(2) and (3)).
- Q.3 *What is the nature of the discretion of the AER to reject what it considers to be an unreasonable proposal?*
- A.3. The AER is given the task of deciding whether the total is a reasonable estimate and is required to take into account twelve factors. The AER is required to assess the probity and veracity of all the evidence presented and may discount weakly supported arguments or assertions. In reaching its decision the AER will be guided by its assessment of the evidence. To the extent to which the factors lead to divergent conclusions, the AER may also be guided by the pricing principles in the National Electricity Law (NEL) which place considerable weight on protecting the interests of service providers.
- Q.4 *Will there be a range of totals that the AER must accept under the AEMC Rule?*
- A.4. Yes. Even by taking into account the twelve factors suggested by the AEMC, the proposed Rule as currently drafted will mean that a range of totals are likely to be a reasonable estimate of expenditure. As the case law explains, given the inherent uncertainty of forecasting and factors which lead to divergent conclusions, a number of different totals may be seen as reasonable.
- Q.5 *What would be the impact of the AEMC's rule at the merits review stage?*
- A.5. Where the AER decided that the total was not a reasonable estimate, and substituted its own figure, the AER would be required to defend its decision that the service provider's estimate was not reasonable and also defend the total figure that the AER decided was a reasonable estimate. If the service provider's estimate was properly rejected by the AER, the discretion for the AER to substitute a reasonable estimate would be broad.
- Where the AER accepted a total, and users considered that it was an overly generous figure, the proposed Rule would make it quite difficult for users to establish that this acceptance should be set aside in merits review.

Q.6. *Would a formulation that required the AER to determine whether the total was the 'best estimate that is reasonably possible in the circumstances' result in the greater discretion for the regulator to reject proposals that it considers to be inefficiently high?*

A.6. Yes. An appropriately worded 'best estimate' test would make it clear that the AER should assess whether the proposal is the optimal total amount and give the AER discretion to substitute a better total when it is not satisfied with that proposed by a service provider. Under such a test (see paragraph 64 of this advice) the AER would still have to consider the proposal and the supporting evidence in the light of what is reasonably possible for a five year forecast. In our view, the AER would be required to accept a narrower range of total forecasts than under the AEMC's approach in the draft Rule. There would still be a 'propose-respond' process, but the decision would be more like a limited 'consider-decide' framework.

However, such a test should not be drafted with qualifying words that could suggest that any reasonable basis may produce a best estimate.

BACKGROUND

Capital and operating expenditure forecasts as part of building block approach

3. This advice concerns the assessment by the AER of future operating and capital expenditure in the regulation of electricity transmission and distribution businesses and may also be relevant to similar issues in gas regulation. The nature of the decision to assess future operating and capital expenditure should be considered in the specific context of the law that deals with this issue. In this case the proposed Rule uses the 'building block' approach to revenue regulation. This approach generally requires 'point estimates' of operating and capital expenditure to be determined for a five year period starting from the time of the determination. For the purposes of achieving incentive regulation, these point estimates are not the actual or most likely estimates for the individual service provider, but are instead designed to be a point estimate of *efficient costs* that should be incurred by the service provider. This idea is captured in s. 8.37 of the current National Third Party Access Code for Natural Gas Pipeline Systems (the Gas Code) which provides that:

A Reference Tariff may provide for the recovery of all Non Capital Costs (or forecast Non Capital Costs, as relevant) except for any such costs that would not be incurred by a prudent Service Provider, acting efficiently, in accordance with accepted and good industry practice, and to achieve the lowest sustainable cost of delivering the Reference Service.

4. You have noted that it is important to recognise that the amounts involved in these future estimates are considerable. The most recent electricity transmission and distribution allowances are set out below.

Distribution	Capex (\$m)	Opex (\$m)	Revenue /price	Transmission	Capex (\$m)	Opex(\$m)	Revenue /price
	Total	Total	Total		Total	Total	Total
ETSA Utilities	753	649	1,862	Electranet	358	261	909
Energex	2,710	1,270	4,418	Powerlink	1,041	524	2,378
Ergon	2,770	1,240	4,208	SP Ausnet	379	396	1,503
AGL	210	260	691	TransGrid	1,188	581	2,415
Citipower	458	177	891	EnergyAustralia	243	122	536
Powercor	796	596	1,788	Transend	307	161	658
SP Ausnet	628	562	1,584	Murraylink interconnect	0	33	124
United Energy	483	419	1,327	Directlink interconnect	0	24	127
EnergyAus	1,548	2,096	4,184	Totals	3,515	2,102	8,648
Integral	1,108	1,416	2,793				
Country Energy	1,201	1,251	3,002				
ActewAGL	191	151	513				
Aurora	270	199	648				
Totals	12,856	10,087	27,261				

5. It is also relevant to note that from information provided to us, none of the totals of the current allowances were the same as the initial proposal submitted by the service provider. Service providers will be required under the AEMC proposed Rule to submit their totals 13 months before the start of the five year period. You note that in past decisions the variation between the initial proposals of service providers and the final allowances used in the building block approach is usually over 10% and sometimes greater than 20%.

AEMC proposed Rule on capital expenditure and operating expenditure

6. As part of its review of Transmission Revenue and Pricing Rules, the AEMC has proposed prescriptive rules which narrowly define almost every aspect of the building block approach to revenue regulation. The AEMC has explained that the purpose of this is to constrain the regulator in a way which the AEMC sees as giving greater certainty to industry. The AEMC has also set out in the proposed Rule detailed considerations for any discretionary decision, essentially on the basis that the NEL objective and pricing principles do not provide sufficient guidance alone, and that the layering of objectives and considerations does not result in substantial uncertainty because the Rules must be designed to achieve the same principles.

7. In this framework the AEMC have proposed the following Rule for arriving at a total of operating expenditure to be used in the building block approach:

6A.6.6 Forecast operating expenditure

(a) A *Revenue Proposal* must include a forecast of the operating expenditure for each *regulatory year* of the relevant *regulatory control period* which the *Transmission Network Service Provider* considers is reasonably required in order to:

- (1) efficiently meet the expected demand for *prescribed transmission services* over that period;
- (2) comply with all applicable *regulatory obligations* associated with the provision of *prescribed transmission services*;
- (3) maintain the quality, reliability and security of supply of *prescribed transmission services*; or
- (4) maintain the reliability, safety and security of the *transmission system* through the supply of *prescribed transmission services*.

(b) The *AER* must accept the forecast operating expenditure for each *regulatory year* as provided under paragraph (a) if:

- (1) the forecast operating expenditure is for expenditure that is properly allocated to *prescribed transmission services* in accordance with the principles and policies set out in the *Cost Allocation Methodology* for the *Transmission Network Service Provider*;
- (2) the total of the forecast operating expenditure for the *regulatory control period* as provided under paragraph (a) is determined by the *AER* to be a reasonable estimate of the *Transmission Network Service Provider's* required operating expenditure for the *regulatory control period*, taking into account:
 - (i) the information included in or accompanying the *Revenue Proposal* or revised proposal;
 - (ii) the need to comply with all applicable *regulatory obligations* associated with the provision of *prescribed transmission services*;
 - (iii) submissions received in the course of consulting on the *Revenue Proposal*;
 - (iv) such analysis as is undertaken by or for the *AER* and is *published* prior to or as part of the draft decision of the *AER* on the *Revenue Proposal* under rule 6A.12 or the final decision of the *AER* on the *Revenue Proposal* under rule 6A.13 (as the case may be);
 - (v) the actual and expected operating expenditure of the provider during any preceding *regulatory control periods*;
 - (vi) the extent to which the forecast operating expenditure of the provider is referable to arrangements with a person other than the provider, that might not be on arm's length terms;
 - (vii) reasonable estimates of the benchmark operating expenditure that would be incurred by an efficient *Transmission Network Service Provider* over the *regulatory control period*;

- (viii) the reasonableness of the demand forecasts on which the forecast operating expenditure is based;
 - (ix) the relative prices of operating and capital inputs;
 - (x) efficiency of substitution possibilities between operating and capital expenditure;
 - (xi) whether the total labour costs included in the capital and operating expenditure forecasts for the *regulatory control period* are consistent with the incentives provided by the *service target performance incentive scheme* that is to apply to the provider in respect of the *regulatory control period*; and
 - (xii) whether the forecast operating expenditure includes amounts relating to a project that should more appropriately be included as a *contingent project* under clause 6A.8.1(b); and
- (3) the operating expenditure forecasts and the information provided in relation to those forecasts, comply with the requirements of the *submission guidelines* made under clause 6A 10.2.

8. The proposed Rule sets up a process for operating expenditure which is mirrored for capital expenditure (proposed Rule 6A.6.7). Accordingly:
- a. the service provider makes a proposal (or a revised proposal) of expenditure *reasonably required* in order to address prescribed matters (proposed Rule 6A.6.6(a) and 6A.6.7(a)); and
 - b. that proposal (or a revised proposal) *must* be accepted by the AER if:
 - it is properly cost allocated (proposed Rule 6A.6.6(b)(1) and 6A.6.7(b)(1));
 - the total of the forecast is determined by the AER to be a reasonable estimate (taking into account prescribed matters) (proposed Rule 6A.6.6(b)(2) and 6A.6.7(b)(3)); and
 - the relevant information complies with AER submission guidelines (proposed Rule 6A.6.6(3) 6A.6.7(b)(4)).
9. There are significant procedural rules in proposed Rule 6A.13.2, 6A.14.1 and 6A.14.3. The relevant procedural rules are at **Attachment A**.
10. In particular under proposed Rule 6A.14.1(2) and (3) both a draft decision and a final decision determines:
- whether the total of the forecast operating or capital expenditure is a reasonable estimate; and
 - if the AER determines that it is not a reasonable estimate, its reasons for that determination and an estimate of the provider's required operating or capital expenditure.

This indicates that the role of the AER is to assess the service provider's proposal and only substitute its own total where the AER determines the totals for operating or capital expenditure in the proposal are not reasonable estimates.

11. Further, proposed Rule 6A.13.2(b) provides that if the AER is not satisfied that the forecast operating or capital expenditure is reasonably required, the AER must include in its final decision the forecast operating or capital expenditure which it determines to be reasonably required.
12. Proposed Rule 6A.14.3 is entitled 'Circumstances in which approval must be given' and indicates that the AER must accept a proposed forecast (including for the purposes of a draft decision, a final decision, and a forecast revised after a draft decision) if the total is determined to be a reasonable estimate (proposed Rule 6A.14.3(b)(5) and (6)). The Rules also set out a presumption that unless the situation has changed, a resubmission by a service provider of a forecast capital or operating expenditure, that is the same as one determined in a draft decision by the AER to be a reasonable estimate, must be accepted (Rule 6A.14.3(c)).

The decision making models generally

13. It is important to put the proposed Rule in the context of the long standing debates about the appropriate level of discretion for a regulator in setting prices for access to essential infrastructure. Given the level of debate and attention that this issue has generated, it is likely to influence the interpretation of the proposed Rule, particularly since the key test revolves around whether or not a forecast is a reasonable estimate.
14. The debate has become increasingly confused as, in addition to a pure propose-respond and a pure consider-decide model, there have developed a limited propose-respond and a limited consider-decide model. A combination of limited propose-respond and limited consider-decide could be regarded as a 'fit for purpose' model as recommended by the Expert Panel. In summary, the models can be distinguished as follows.

Pure propose-respond

15. A pure propose-respond model involves the service provider developing all crucial elements of an access arrangement for that service provider, and the regulator is then asked to accept those proposed terms and conditions. The regulator must do so if they are within the bounds of a high level legal framework and are overall reasonable. If they do not comply with the framework or are not reasonable, the regulator then develops its own access arrangement to remedy the deficiencies.

Pure consider-decide

16. A pure consider-decide model gives the regulator the power to decide the core terms and conditions of access for a service provider based on high level legal

principles and after considering various proposals from the service provider about what terms and conditions should be applicable. Part B of Chapter 6 of the current National Electricity Rules (based on the National Electricity Code) is such a model. This model has also been referred to as a 'receive-determine' or 'submit-determine' model.

Limited propose-respond

17. A limited propose-respond model requires particular aspects of a service provider's access proposal to be accepted if they comply with a test specified in the relevant law. If that test is not satisfied, the regulator can substitute its own view when finalising the terms and conditions of access. Nonetheless, the key feature of this model, as well as the pure propose-respond model, is that the regulator cannot substitute a term, condition or figure that meets the requirements of the relevant law simply because it prefers another term, condition or figure and thinks that term, condition or figure will better meet the objects of the relevant law.

Limited consider-decide

18. A limited consider-decide model is one where particular aspects of the regulator's discretion are highly constrained by the framework of the relevant law, but the regulator retains the ability to determine an outcome that best meets the requirements of the law.

Implications

19. You have asked that the proposed Rule be analysed as to whether it allows the forecast operating and capital expenditure to be determined:
 - a. by what the regulator considers to be the best, optimal or most appropriate estimate (the limited consider-decide model); or
 - b. by first considering if the service providers proposal is within a range of reasonable outcomes (in which case it must be accepted) and only allowing the regulator to decide the estimate when the service provider's total is outside of that reasonable range (the limited propose-respond model).

INTERPRETING THE AEMC PROPOSED RULE

Words of the proposed Rule.

20. In our view the relevant terms of the proposed Rule itself, which we have set out above, suggest that it follows the limited propose-respond model. In relation to the elements of operational and capital expenditure, the service provider makes a proposal which must be accepted by the AER if the total of the forecast is determined by the AER to be a reasonable estimate (taking into account prescribed matters) (proposed Rule 6A.6.6(b)(2) and 6A.6.7(b)(3)). The role of the AER is to assess the service provider's proposal and only substitute its own total where the AER determines the totals for operating or capital expenditure in the proposal are

not reasonable estimates (proposed Rule 6A.14.1 and 6A.14.3). That is this aspect of the service provider's proposal must be accepted if it complies with the test of a 'reasonable estimate' and only if that test is not satisfied can the AER substitute its own view.

Case law underpinning the propose-respond model

- 21. The recognition of the propose-respond model in decisions of the Australian Competition Tribunal and Federal Court should also be considered for their assistance in interpreting the proposed Rule.

Gasnet

- 22. The Australian Competition Tribunal decision in *Application by GasNet Australia (Operations) Pty Ltd* [2003] ACompT 6 (23 December 2003) (*Gasnet*) is important in this regard. That decision took the process of submission and approval of an access arrangement in s. 2.24 of the Gas Code, combined with the recognition in the Western Australian case of *Re Michael; Ex parte Epic Energy (WA) Nominees Pty Ltd* (2002) 25 WAR 511 (*Michael*) that the principles for setting a tariff in the Gas Code may come into conflict, and concluded (emphasis added):

[29] It is clear in the reasoning in *Michael* that there is no single correct figure involved in determining the values of the parameters to be applied in developing an applicable Reference Tariff. The application of the Reference Tariff Principles involves issues of judgment and degree. **Different minds, acting reasonably, can be expected to make different choices within a range of possible choices which nonetheless remain consistent with the Reference Tariff Principles.** Where the Reference Tariff Principles produce tension, the Relevant Regulator has an overriding discretion to resolve the tensions in a way which best reflects the statutory objectives of the Law. However, where there are no conflicts or tensions in the application of the Reference Tariff Principles, and where the AA proposed by the Service Provider falls within the range of choice reasonably open and consistent with Reference Tariff Principles, **it is beyond the power of the Relevant Regulator not to approve the proposed AA simply because it prefers a different AA which it believes would better achieve the Relevant Regulator's understanding of the statutory objectives of the Law.**

[30] This follows because the power of the Relevant Regulator to require amendments, or to itself draft and approve its own AA, does not arise until it is of the opinion that the AA proposed by the Service Provider does not comply with the Code, and in determining the question of compliance, it must act in accordance with s 2.24 of the Code.

- 23. This conclusion was essentially based on the requirement in s. 2.24 of the Gas Code that the regulator 'may approve' an access arrangement 'only if it is satisfied' the arrangement contains the required elements in chapter 3 of the Gas Code. That decision must take into account the factors in s. 2.24. That decision involves, as discussed in *Gasnet*, a propose-respond model.

24. The Full Federal Court confirmed this understanding of the Gas Code in *ACCC v Australian Competition Tribunal* [2006] FCAFC 83 (2 June 2006) by directly agreeing with the proposition in *Gasnet* as follows:

[165] In assessing an Access Arrangement proposal and deciding whether to approve it or not, the ACCC is not at large simply to substitute its own preferred Access Arrangement. In *Application by GasNet Australia (Operations) Pty Ltd* (2004) ATPR 41-978 the Tribunal, on which Cooper J presided, held that it was beyond the power of the ACCC as Relevant Regulator not to approve a proposed Access Arrangement simply because it preferred a different Access Arrangement which it thought could better achieve the statutory objectives:

[30] This follows because the power of the Relevant Regulator to require amendments, or to itself draft and approve its own AA, does not arise until it is of the opinion that the AA proposed by the Service Provider does not comply with the Code, and in determining the question of compliance, it must act in accordance with s 2.24 of the Code.'

This conclusion follows from the language of the Code. But once the threshold of non-approval is properly crossed, the ACCC is at large in the content of its own Access Arrangement albeit it must be within the framework provided by the Code.

Telstra

25. The recent consideration of access undertakings in relation to telecommunications is also relevant. In *Telstra Corporation Limited* [2006] ACompT 4 (2 June 2006) (*Telstra*) the key principles from *Gasnet* have been imported into the requirements for the ACCC to accept access arrangements under Part XIC of the *Trade Practices Act 1974*. It is noted that in relation to telecommunications the criteria for accepting undertakings are set out in s.152CBD which provides in part:

- (2) The Commission must not accept the undertaking unless:

...

- (b) the Commission is satisfied that those terms and conditions are reasonable; and

Section 152AH then provides:

152AH Reasonableness—terms and conditions

- (1) For the purposes of this Part, in determining whether particular terms and conditions are reasonable, regard must be had to the following matters:
- (a) whether the terms and conditions promote the long-term interests of end-users of carriage services or of services supplied by means of carriage services;
 - (b) the legitimate business interests of the carrier or carriage service provider concerned, and the carrier's or provider's investment in facilities used to supply the declared service concerned;
 - (c) the interests of persons who have rights to use the declared service concerned;
 - (d) the direct costs of providing access to the declared service concerned;

- (e) the operational and technical requirements necessary for the safe and reliable operation of a carriage service, a telecommunications network or a facility;
- (f) the economically efficient operation of a carriage service, a telecommunications network or a facility.

(2) Subsection (1) does not, by implication, limit the matters to which regard may be had.

26. In *Telstra*, the Australian Competition Tribunal interpreted these provisions as follows (emphasis added):

[62] Telstra's principal contention was that the \$9.00 monthly charge was reasonable so long as it did not exceed what it claimed to be the efficient costs of supply of the LSS, namely \$11.75 being the \$10.98 per LSS line per month plus the \$0.77 it contended was the share of network costs attributed to its LSS.

[63] Telstra submitted that a term relating to the price charged by an access provider will be reasonable if the price will permit the access provider to recover no more than a reasonable estimate of the efficient costs of delivering that service during the period of an undertaking. Insofar as Telstra's submission is tied to the period of the undertaking, a period it alone controls, we do not accept that submission (see par [107] below). **In this area of analysis there is no one correct or appropriate figure in determining reasonable costs or a reasonable charge. Matters and issues of judgment and degree are involved at various levels of the analysis.** In considering whether Telstra's estimates of its costs are reasonable we are not driven to considering whether the Commission's or other parties' views or assessment of those costs are more reasonable. Nor do we enquire whether Telstra's method or approach in estimating its costs is the correct or appropriate approach. If Telstra's method or approach in estimating its costs is reasonable having regard to the statutory matters set out in ss 152AH and 152AB then the matter rests and a comparison with the \$9.00 monthly charge is then to be made: *Application by GasNet Australia (Operations) Pty Ltd* (2004) ATPR 41-978 at [29]. Put shortly, our inquiry is whether the method employed by Telstra at each level of determining the costs of its LSS is reasonable having regard to the statutory matters identified in s 152AH and the objectives set out in s 152AB.

[64] It is clear that the relevant inquiry brings into consideration the matters set out in ss 152AH and 152AB of the Act. For in determining whether a term relating to price is reasonable, regard must be had to the matters set out in those sections. As Telstra acknowledged, in coming to a decision whether or not a term relating to a price or charge is reasonable **it is necessary for the Tribunal to look at the means by which the price or charge was derived and to consider whether the method adopted was, in the circumstances, reasonable.** That, in turn, requires evaluating the method adopted by reference to the same matters set out in ss 152AH and 152AB.

...

[67] ...the relevant inquiry is whether Telstra's \$9.00 monthly charge is reasonable having regard to the matters set out in ss 152AH and 152AB of the Act. If we find that that charge and the principles by which its relevant components are determined are reasonable having regard to those matters, then it does not matter whether there may be a period of levelisation of the annual costs, other than the period chosen by Telstra, which may also be thought to be reasonable. Nor does it matter whether there may be a cost allocation over services different from that chosen by Telstra which may be

regarded as reasonable. **In a number of respects we are operating in areas where there is no one specific regulatory, economic, accounting or financial answer, and where there may be a number of approaches to the determination of relevant costs or their allocation which may be regarded as reasonable.** Our inquiry is directed to whether Telstra's \$9.00 monthly charge in its access undertaking is reasonable having regard to the statutory matters set out in of ss 152AH and 152AB of the Act.

[68] We should also point out that when ss 152AH and 152AB require the Tribunal to have "regard" to certain matters, the Tribunal is required, in the words of Mason J, to take those matters into account and to give weight to them as fundamental elements in making its determination: *The Queen v Hunt; Ex parte Sean Investments Pty Ltd* (1979) 180 CLR 322 at 329.

This decision discusses the telecommunications provisions within the propose-respond model.

Summary of case law

27. The key themes from these interpretations of the Gas Code and Trade Practices Act provisions are as follows.
 - a. Where legislation requires a party to submit an access proposal and requires the regulator to accept or approve that proposal if it complies with a particular test, the regulator will be bound to accept a proposal if it is within the range of acceptable outcomes allowed by the particular test.
 - b. Accordingly, a regulator cannot substitute a term, condition or figure that it considers better achieves the statutory objectives if a proposed term, condition or figure is consistent with the range of acceptable outcomes.
 - c. A regulator will be assisted by lists of factors that help decide what will be an acceptable outcome, but the nature of determining future access arrangements necessarily implies that a number of different approaches will comply with the factors.
 - d. Once a threshold for rejection is reached, the regulator is at large (within the confines of the relevant law) with respect to imposing a more appropriate result on the service provider; and
 - e. Tribunals and Courts will be called to examine both the decision of the regulator to reject a proposal (the threshold for rejection) and the imposition of an alternative by the regulator after that threshold has been established.

Key implications for proposed Rule

28. The essential framework of the proposed Rule discussed above mirrors the concepts in the Gas Code (where an access arrangement is assessed for its compliance with the Code) and Part IXC of the Trade Practices Act (where the proposed access undertakings terms and conditions must be approved if the regulator is satisfied they are reasonable taking into account a number of factors).

As such the proposed Rule is a further development of the propose-respond model. The logic of the propose-respond model inherent in these decisions is translatable across to the proposed Rule. The proposed Rule clearly recognises that:

- a. a range of total forecasts proposed by the service provider will need to be accepted by the AER;
- b. the AER cannot just prefer a different forecast without finding that the proposal is not a reasonable estimate; and
- c. the AER's task of determining whether a service provider has proposed a reasonable estimate is guided by the twelve factors in the proposed Rule.

In our view the proposed Rule is therefore a limited propose-respond decision making model. If anything, the 'must accept' wording of the proposed Rule makes this clearer than the Gas Code's formulation of 'may approve ... only if' or the telecommunications wording of 'must not accept ... unless'.

AEMC Draft Determination

29. The terms of the AEMC Draft Rule Determination reinforces the interpretation of the proposed Rule as a limited propose-respond decision rule where the regulator will be required to accept a range of possible totals when it states at p 51-52 (emphasis added):

The Commission agrees with the comments of the Australian Competition Tribunal in a number of recent cases, including the GasNet decision and the recent Telstra decision, that in areas of economic regulation where the subject matter is such that **there is no 'correct' answer and in respect of which reasonably qualified experts would vary in opinion, the task of the regulator is to make a 'reasonable' decision, not the 'best' decision.**

That approach is of particular relevance when the subject matter of a regulatory decision is the allowable forecast operating and capital expenditure for a large and complex business such as a TNSP over a five year period. The resolution of such forecasts requires the exercise of judgement about the level of future demand, both in general and specific terms, about the likely scale and timing of various market developments and about the likely variation of costs of inputs in that period.

In these circumstances the Commission has concluded that the TNSP and AER should strive for determination of a 'reasonable estimate' of future expenditure, subject to guidance in the Rules as to the criteria and evidentiary factors that should be considered in reaching that judgement. **Any attempt to identify the 'best' estimate in these circumstances is unachievable and involves the risk of regulatory error.** The Commission reiterates, however, that the reasonable estimate decision rule confers on the AER the responsibility for making the determination of whether the forecasts represent reasonable estimates, having regard to the guidance provided by the relevant decision criteria.

Regarding the Expert Panel's concern about the potential for uncertainty regarding the interpretation of the reasonable estimate decision test, the Commission notes that some uncertainty is necessarily associated with the interpretation of any decision criterion, including the 'best estimate arrived at on a reasonable basis' that is preferred by the

Panel. However, the Commission considers that any uncertainty of interpretation of the reasonable estimate criterion will be reduced substantially by the requirement for the AER to have regard to the criteria and evidentiary material specified in the Rules. It notes in this regard that the AER has commented that the list of factors to be considered provides an appropriate basis for the assessment of expenditure forecasts and its concern is with the decision rule itself.

30. We note that there is some uncertainty as to the ability of a regulator, court or tribunal to use extrinsic materials in interpreting the National Electricity Rules. Item 8 of Schedule 2 of the NEL allows for the use of extrinsic materials in relation to the interpretation of a provision of the Law. Item 41 provides that the Schedule applies to a statutory instrument in the same way as it applies to the Law, and this may include the Rules. However, clause 1.7 of the Rules provides that only specified provisions of Schedule 2 of the NEL apply to the Rules, and item 8 is not specified. We understand that proposed NEL and Rules amendments will clarify the application of items 7 and 8 of Schedule 2 of the NEL to the Rules and the relevance of AEMC Rule Determinations as an extrinsic material that can be considered to assist interpretation of the Rules. Even before such amendments it may be possible to argue that under general interpretation principles, regard can be had to extrinsic materials in interpreting Rule changes, especially to resolve ambiguities.
31. The effect of the AEMC statement confirms the applicability of the logic in the *Gasnet* and *Telstra* decisions that the nature of forecasting future expenditure means that a range of forecasts will fall within the concept of a reasonable estimate.

CONSTRAINTS ON WHAT THE AER MUST ACCEPT

32. You have asked us about the 'reasonable estimate' test which the AER will need to apply. It is important to give particular consideration to the interpretation of the words and factors used in the proposed Rule to determine where the threshold of acceptance will lie.

The meaning of what is a 'reasonable estimate'

33. The words 'reasonable estimate' must be given their ordinary meaning in the context of the proposed Rule. While various judicial considerations of what is reasonable may be of assistance, these will not be determinative of the special meaning to be attributed to the phrase in this context. The *Macquarie Dictionary* provides four definitions of 'reasonable':
1. endowed with reason.
 2. agreeable to reason or sound judgment: *a reasonable choice*.
 3. not exceeding the limits prescribed by reason; not excessive.
 4. moderate, or moderate in price: *the coat was reasonable but not cheap*.

In our view, meanings 2 and 3 are the most relevant.

34. Similarly, the *Macquarie Dictionary* defines an 'estimate' as follows:

1. to form an approximate judgement or opinion regarding the value, amount, size, weight, etc., of; calculate approximately. 2. to form an opinion of; judge. 3. to submit approximate figures, as of the cost of work to be done. 4. an approximate judgement or calculation, as of the value, amount, etc., of something. 5. a judgement or opinion, as of the qualities of a person or thing; estimation or judgement. 6. an approximate statement of what would be charged for certain work to be done, submitted by one ready to undertake the work.

In our view, meanings 1 and 4 are the most relevant.

35. The concept of an 'estimate' as an approximation is picked up by the following comments of Hill J in *Australia and New Zealand Banking Group Ltd v FCT* (1994) 119 ALR 727 at 741:

The concept of "estimate" does not involve arbitrarily seizing upon any figure. What is involved is the formation of a judgment or opinion based upon reason. That judgment or opinion must necessarily be made bona fide but it need not be exact for the process of estimation involves a process of approximation. As Lord Loreburn said in *Sun Insurance Office v Clark* (1912) AC 443 at 454:

"There is no rule of law as to the proper way of making an estimate. There is no way of estimating what is right or wrong in itself. It is a question of fact and figures whether the way of making the estimate in any case is the best way for that case."

36. The concept of a 'reasonable estimate' must therefore encompass the idea of an approximation of future costs which is open on the facts and based upon reason, or at least does not exceed the limits prescribed by reason. It may also be relevant that the AER is to determine whether the total of a 'forecast' is a reasonable estimate, and the word 'forecast' further reflects the idea of a prediction, and conjecture as to the future.
37. Judicial commentary on various tests of 'reasonable' provides some examples of what sort of estimates can be rejected as not reasonable without completely clarifying what must be considered reasonable. It is clear that the standard is not related to the judicial review standard of *Wednesbury* unreasonable, that is so unreasonable that no reasonable person could reach the decision (see *Associated Provincial Picture House Ltd v Wednesbury Corporation* [1948] 1 KB 223; *Minister for Immigration and Multicultural Affairs v Eshetu* (1999) 197 CLR 611).
38. Some assistance may be taken from the Full Federal Court's interpretation of the 'unreasonable' merits review ground in the Gas Pipelines Access Law in *ACCC v Australian Competition Tribunal* [2006] FCAFC 83 at [177] - [178]. Accordingly, by analogy, an estimate would be unreasonable where there is:
- a. a logical error or irrationality in the reasoning;
 - b. a want of reason such that a figure is not justified by its stated reasons;
 - c. some discontinuity or *non sequitur* in reasoning; or

- d. an element of arbitrariness about it because of an absence of reason to explain the choices made by the service provider in arriving at its total.
39. In other contexts Brennan J, considering what a 'reasonable hypothesis' would entail in *Bushell v Repatriation Commission* (1992) 175 CLR 408 at 428, approved the distinction drawn in *Repatriation Commission v Webb* (1987) 76 ALR 131 at 135 between 'a theory that is rationally based' and one that is 'irrational, absurd or ridiculous'.
40. A similar theme comes through in the context of reasonable grounds to issue conclusive certificates in freedom of information matters. In *Department of Industrial Relations v Burchill* (1991) 33 FCR 122, Davies J. (at 125-126) endorsed the following approach as to what constitutes 'reasonable' grounds:
- To be 'reasonable', it is requisite only that they be not fanciful, imaginary or contrived, but rather that they be reasonable; that is to say based on reason, namely agreeable to reason, not irrational, absurd or ridiculous.
41. However, Hayne J in the recent High Court decision in *McKinnon v Secretary, Department of Treasury* [2006] HCA 45 (6 September 2006) at [60] warned against treating various paraphrases of 'unreasonable' as supplanting the actual words of the statute. He stated:
- The expression "not irrational, absurd or ridiculous" is not synonymous with "reasonable grounds". Of course, absurd, irrational or ridiculous grounds are not reasonable grounds. But the words "reasonable grounds" do not denote grounds which are "not irrational, absurd or ridiculous". The statutory words are to be given their ordinary meaning. It will seldom be helpful, and it will often be misleading, to adopt some paraphrase of them.
42. Nonetheless, the ordinary meaning of a 'reasonable estimate', the various judicial interpretations of 'reasonable' and the current trend of access regulation case law (i.e. *Gasnet* and *Telstra*), confirms that there will be a number of total forecasts that are 'reasonably' open to the service provider, and will necessarily have to be accepted by the AER under the proposed Rule.
43. Additionally, the concept of 'reasonable estimate' should not be confused with the concept of a 'reasonable range' of outcomes, within which a forecast must fall. The proposed Rule simply asks whether a particular total is a reasonable estimate. The proposed Rule is not as broad as the Productivity Commission's approach of an estimate only needing to be within 'a range of plausible outcomes'. As the proposed Rule is not based around the AER's view of the best or most statistically probable total there will be a number of different outcomes which will be considered to be reasonable estimates. It is impossible to accurately predict, from a legal point of view, how wide that range of outcomes will be given the nature of the decisions in question.

The role of the twelve factors

44. It is important to understand the AER's task of determining whether or not the total of a forecast is reasonable is given additional meaning by the twelve factors listed in the proposed Rule. These factors will ensure that the AER undertakes a detailed examination of all aspects of a service provider's proposal. The AER will need to weigh up the merits of the forecasts, claims and assumptions on which that total is based. This will guide the AER in determining if the service provider's costs are reasonably required for the reasons in paragraph (a) of 6A.6.6. As explained in *Michael* the obligation to 'take into account' the factors is a fundamental element in making the AER's decision (at [55]).
45. The factors are a mix of process requirements and other assessments of information, types of analysis or relationships. Taking them into account does not mean that all of the evidence must be accepted at face value or as true.
46. The AER will also have the key task of giving weight to the divergent considerations: see *Minister for Aboriginal Affairs v Peko Wallsend* (1986) 162 CLR 24 at 41. The explicit recognition of this fact at the end of s. 8.1 of the Gas Code is not present in the proposed Rule.
47. Nonetheless, the nature of forecasting an efficient level of expenditure and the inherent uncertainty associated with predicting future demand and trends will inevitably lead the consideration of the factors to pull in different directions. For instance:
 - the service provider will have an incentive to submit and justify a generous proposal (factor (i));
 - submissions may challenge this, with users presenting an overly cautious view (factor (iii));
 - published AER expert analysis may suggest a lower figure for several discrete elements or projects which is later challenged by expert reports from the service provider (factor (iv));
 - actual expenditure during the previous period may be lower than expected, but evidence may be presented that the efficiency gains are unsustainable (factor (v));
 - contractual arrangements might be different from normal industry practice, but these may be the result of arms length negotiations (factor (vi));
 - benchmarking analysis may indicate that the service provider is operating at an inefficient level, but this may be questioned because of problems with adequate data for productivity based assessments (factor (vii)); and
 - demand forecasts may be provided on a number of bases by different parties, and inevitably these may depend on other extraneous events. The AER's

assessment of the 'reasonableness' of various demand forecasts may also lead to a range of outcomes (factor (viii)).

48. The probity and veracity of the evidence relating to these factors will obviously be the most important elements in the AER's view of whether the total is a reasonable estimate. There will be issues of materiality in whether doubt on one element or figure deprives the total proposed by the service provider of being a reasonable estimate. The list of factors will necessarily bring reasonably held propositions and positions into conflict.

Role of the NEL objective and pricing principles

49. Relevantly, after the proposed NEL amendments, both the Expert Panel pricing principles and the new objective of the NEL may be relevant in assisting the AER resolve conflicts between the factors in the proposed Rule. This would follow from the logic in *Michael* where conflicts within list of factors in particular provisions (such as determination of an initial capital base in ss. 8.10 and 8.11 of the Gas Code) needed to be resolved by reference to objectives outside of those provisions (that is the reference tariff principles in s. 8.1). Similarly 'guidance in the exercise of discretion to resolve conflict within s. 8.1 will be provided from outside that provision', that is in s. 2.24 of the Gas Code (see [136]). On the other hand, a court or tribunal may find that the evidentiary factors in the proposed Rule are so comprehensive and different to the policy based considerations in ss. 8.1, 8.10 and 8.11 of the Gas Code that there is little room for broader principles to provide any further guidance.

50. Section 16 of the NEL will continue to require the AER to carry out its economic regulatory functions in a manner which will, or is likely to, contribute to the achievement of the NEL objective. The new NEL objective will provide that:

The objective of this law is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to price, quality, reliability and security of supply of electricity and the reliability, safety and security of the national electricity system.

51. The AER will also be required by the NEL to take into account the following pricing principles when exercising a discretion in making a network revenue or pricing determination:

- (1) provide a reasonable opportunity for a network operator to recover at least the efficient costs of providing services that are the subject of the network pricing determination and complying with a regulatory obligation; and
- (2) provide effective incentives to a network operator to promote economic efficiency in the provision by it of services that are the subject of a network pricing determination, including:
 - (i) the making of efficient investments in the network owned, controlled or operated by it and used to provide services that are the subject of a network pricing determination;

- (ii) the efficient provision by it of services that are the subject of a network pricing determination; and
 - (iii) the making of efficient use of existing assets and proposed new assets that are, or are to be, used to provide services that are the subject of a network pricing determination;
- (3) make allowance for the value of assets forming part of a network owned, controlled or operated by a network operator, and the value of proposed new assets to form part of that network, that are, or are to be, used to provide services that are the subject of a network pricing determination;
- (4) have regard to any valuation of assets forming part of a transmission or distribution system owned, controlled or operated by a network operator applied in any relevant determination or decision; and
- (5) have regard to the economic costs and risks of:
- (i) the potential for under-investment and over-investment in assets by the network operator; and
 - (ii) the potential for under-utilisation and over-utilisation of the capacity of assets forming part of a distribution or transmission system, and the capacity of proposed new assets.
52. The NEL objective and the pricing principles may influence the resolution of uncertainty with regard to a service provider's estimates. We note that these in turn also contain competing objectives and considerations. However, generally the pricing principles place considerable weight on protecting the interests of service providers. The pricing principles in particular would therefore favour the view that a broad range of proposals from a service provider will be within the bounds of a reasonable estimate.

Conclusion on interpreting what will be a 'reasonable estimate'

53. The reasonable estimate decision framework based on the twelve factors does enable the AER to reject total forecasts which are not based upon reason, or exceed the limits prescribed by reason, after critically analysing all the evidence. However, the use of the 'reasonable estimate' test, uncertainty in forecasting, the existing case law in *Gasnet* and *Telstra* and the role of the pricing principles in resolving conflict, will result in the AER being required to accept a range of forecasts higher than those it would determine as the most appropriate or best estimate.

IMPLICATIONS FOR MERITS REVIEW

How would the proposed Rule operate in merits review?

54. Amendments to the NEL will enable limited merits review of the AER's decisions regarding:
- a. whether or not a total forecast is reasonable (threshold question); and

- b. its own reasonable estimate, if it decides that the service provider's total is not reasonable.
55. Any applicant for merits review will be limited to the evidence before the AER in making out a ground of review and will need to establish that:
- (a) the original decision maker made an error of fact in its findings of facts, and that error of fact was material to the making of the decision;
 - (b) the original decision maker made more than one error of fact in its findings of facts, and that those errors of fact, in combination, were material to the making of the decision;
 - (c) the exercise of the original decision maker's discretion was incorrect, having regard to all the circumstances;
 - (d) the original decision maker's decision was unreasonable, having regard to all the circumstances.
56. These grounds are expected to retain the meaning set out by the Full Federal Court in interpreting essentially the same grounds in the Gas Pipelines Access Law in *ACCC v Australian Competition Tribunal* [2006] FCAFC 83 at [169] to [180]. Accordingly the finding of fact grounds (a) and (b) will include:
- 1. the existence of an historical fact being an event or circumstance;
 - 2. the existence of a present fact being an event or circumstance; and
 - 3. an opinion about the existence of a future fact or circumstance.
57. The Full Federal Court made clear that the third aspect of facts 'should encompass opinions formed by the ACCC based upon approaches to the assessment of facts or methodologies which it has chosen to apply' (at [171]). Accordingly, the Tribunal may examine the AER's findings of future facts relating to expenditure and demand relevant to the decision that a total forecast is not reasonable, and the determination of the AER's own estimate. Those errors, or cumulative errors will need to be material to the decision, but the nature of the operative and capital expenditure forecasts are by their very nature likely to reach that threshold. It is also the case that the applicant for review will be able to choose which future fact or circumstance it wishes to dispute, and it will then be up to the AER or other interested parties to raise issues with other findings of fact.
58. The Full Federal Court at [176] also made it clear that the Tribunal when considering whether the 'incorrect' or 'unreasonable' grounds (which will be (c) and (d) above) are made out, has to do more than simply prefer a different outcome to overturn the regulator's discretion. However, the Full Federal Court rejected the argument that the unreasonable ground was limited to *Wednesbury* unreasonableness (at [177]).
59. The highly factual nature of the decision and the large number of factors the AER must take into account will mean that a decision to reject a total because it is not a reasonable estimate and the imposition of a new total will be subject to considerable

scrutiny in merits review. Given that the regulator's decision to impose its own estimate only needs to be what it considers 'reasonable', a service provider's application would probably focus on the initial threshold rejection decision rather than the new total, as has been the trend of recent reviews under the Gas Code. The Full Federal Court even noted that 'once the threshold of non-approval is properly crossed, the ACCC is at large in the content of its own Access Arrangement albeit it must be within the framework provided by the Code' at [165]. This position can be seen as part of the incentive for a service provider in a propose-respond framework.

60. The situation where the AER accepts a generous proposal from a service provider also needs to be considered. Users may wish to challenge that the AER's decision. In such a case, the Tribunal may focus on distinguishing a 'reasonable' estimate, from the absurd, irrational or ridiculous, if the AER has formed a *bona fide* view of the total. The current limited merits review framework, including the threat of indemnity costs, would make such review difficult for any applicant.

MODIFICATIONS TO THE AEMC RULE

Would a burden of proof change the analysis?

61. The proposed Rule does not impose any particular burden of proof on the AER to demonstrate or prove the forecast is not a reasonable estimate, or on the service provider to prove that it is. In a way similar to that for authorisations under Part VII of the Trade Practices Act no legal concept of an onus of proof is likely to be read into the Rules (*Re Tooth & Co Ltd; Re Tooheys Ltd* (1979) 39 FLR 1). The AER must simply make a decision on the factors and set out its reasons for that decision. This may be different if the introductory words were closer to the telecommunications test of 'must not accept ... unless ... satisfied' which could result in an onus on the service provider to satisfy the AER of the reasonableness of the total under the proposed Rule (see *Telstra* at [20]) rather than the formulation of 'must accept' in the proposed Rule.
62. However, altering the drafting of the proposed Rule so that the service provider must prove the total to be a reasonable estimate would not significantly alter the reasoning above. There will still be a range of acceptable outcomes and uncertainty in the results of the analysis presented under each of the factors.

How would a criteria of 'best estimate' alter the decision making framework?

63. It has been suggested that the proposed Rule could be amended to refer to the AER being satisfied that the forecast is the 'best estimate arrived at on a reasonable basis' consistent with the views of the Expert Panel (see page 83 of their Report). The idea of the AER determining whether a total is the 'best estimate' moves away from the breadth of reasonable estimates that the AER will be required to accept under the proposed Rule.

64. The words 'arrived at on a reasonable basis' do however create some ambiguity as to what should be examined to reach a best estimate. They could be interpreted as implying that the enquiry should simply focus on whether any reasonable basis can be shown to support an estimate which must then be accepted. We do not think that this is the interpretation understood by the Expert Panel in their Report. Instead it appears that what is meant by the alternative criteria is that the AER must accept a forecast if it is satisfied that the total:
- is the best estimate that is reasonably possible in the circumstances; and
 - is arrived at on a reasonable basis;
- having regard to the factors in the proposed Rule.
65. If the AER decided that a forecast is not the best estimate reasonably possible, it would be obliged to substitute a total it considered to be the best estimate, and not just a reasonable estimate.
66. Being satisfied that the forecast is the best estimate would involve the AER coming to a view on the most appropriate point estimate reasonably possible for the forecast having regard to the twelve factors. The issues of uncertainty would still need to be resolved on the basis of the evidence before the AER and with guidance from the pricing principles, in particular that the service provider should be able to recover at least its efficient costs. The AER would still need to pay due attention to the service provider's inherent understanding of their own business environment, and weigh that up against its own understanding of efficient costing that will arise from its regulation of the other 43 electricity and gas businesses in Australia. The idea of the estimate being one which is also arrived at on a 'reasonable basis' recognises that there will be inherent difficulties in setting an overall future allowance, but that the total needs to be soundly supported.
67. Given that the factors are to remain the same under both models, and that the AER will be required to undertake a very thorough analysis to determine whether the total of a forecast is a reasonable estimate, or the best estimate, the work required of the AER, and the information required, will be essentially the same under both models.
68. The AER's discretion both to accept a total as a best estimate, or impose a best estimate, will result in more symmetrical review rights for users and service providers as opposed to a test based on a reasonable estimate.
69. The best estimate model may still be considered, to some extent, a limited propose-respond model in process terms. However, the decision making rule is much closer to a 'limited consider-decide' model. The key is that the AER can prefer a better estimate to that of the service provider, even when the service provider's proposal is within the bounds of a reasonable estimate.
70. We also note that the Rule could simply give the AER the task of setting an allowance for capital and operating expenditure having regard to the specified

factors. This would be a much clearer consider-decide model and would avoid the possibility of the *Gasnet* principles being read into the Rule.

71. Additionally, we note that this advice is based on the current proposed Rule, the draft rule determination and explanatory materials. Any changes may impact on our analysis. We would be happy to provide further advice after the final rule determination. Please contact us if you have any questions.

Yours sincerely

Robert Orr QC
Deputy General Counsel

Peter Nicholas
Counsel

Attachment A

Procedural rules relevant to Operating and Capital Expenditure

6A.13.2 Refusal to approve amounts, values or framework

(a) If the AER's final decision is to refuse to approve an amount or value referred to in clause 6A.14.1(1), the AER must include in its final decision a substitute amount or value which, except as provided in clause 6A.13.2(b), is:

- (1) determined on the basis of the current Revenue Proposal; and
- (2) amended from that basis only to the extent necessary to enable it to be approved in accordance with the Rules.

(b) If the AER's final decision is to refuse to approve an amount or value referred to in clause 6A.14.1(1) for the reason that, or a reason which includes the reason that, the AER is not satisfied that:

- (1) the forecast operating expenditure for any regulatory year is reasonably required for the purposes set out in clause 6A.6.6(a) (the AER not being otherwise required to accept that forecast operating expenditure under clause 6A.6.6(b)); or
- (2) the forecast capital expenditure for any regulatory year is reasonably required for the purposes set out in clause 6A.6.7(a) (the AER not being otherwise required to accept that forecast capital expenditure under clause 6A.6.7(b)),

the AER must:

- (3) include in its final decision the forecast operating or capital expenditure for that regulatory year (as the case may be) which it determines to be reasonably required for the purposes set out in clause 6A.6.6(a) or 6A.6.7(a) respectively; and
- (4) must use that amount (and its components) in place of the forecast capital or operating expenditure for that regulatory year contained in the current Revenue Proposal for the purposes of calculating the amount or value that it has refused to approve in its final decision.

6A.14.1 Contents of decisions

A draft decision under rule 6A.12 or a final decision under rule 6A.13 is a decision by the AER:

...

(2) in which the AER determines:

- (i) whether the total of the forecast capital expenditure for the regulatory control period as set out in the current Revenue Proposal is a reasonable estimate of the Transmission Network Service Provider's required capital expenditure for the regulatory control period, taking into account the matters referred to in clause 6A.6.7(b)(3); and
- (ii) (if the AER determines that it is not a reasonable estimate), its reasons for that determination and an estimate of the provider's required capital expenditure for the regulatory control period that the AER considers to be reasonable, taking into account the matters referred to in clause 6A.6.7(b)(3), together with the reasons for that conclusion;

(Note that (3) is the same for operating expenditure)

6A.14.3 Circumstances in which approval must be given

(a) This clause set out the circumstances in which the AER must approve certain matters for the purposes of a draft decision under rule 6A.12 or final decision under rule 6A.13. If the AER is not required to approve such a matter in accordance with this clause, it may, but is not required to, refuse to approve that matter.

(b) The AER must approve:

- (1) the total revenue cap for a Transmission Network Service Provider for a regulatory control period; and
- (2) the maximum allowed revenue for the provider for each regulatory year of the regulatory control period,

as set out in the current Revenue Proposal, if the AER is satisfied that:

- (3) those amounts have been properly calculated using the post-tax revenue model;
- (4) those amounts, and any amount required to be calculated or determined for the purposes of calculating those amounts, have otherwise been calculated or determined in accordance with the requirements of Part C;
- (5) the total of the forecast capital expenditure for the regulatory control period as set out in the current Revenue Proposal is a reasonable estimate of the provider's required capital expenditure for the regulatory control period, taking into account the matters listed in clause 6A.6.7(b); and
- (6) the total of the forecast operating expenditure for the regulatory control period as set out in the current Revenue Proposal is a reasonable estimate of the provider's required operating expenditure for the regulatory control period, taking into account the matters listed in clause 6A.6.6(b).

(c) If a Transmission Network Service Provider's revised Revenue Proposal submitted under clause 6A.12.3(a) includes:

- (1) an amount of total forecast capital expenditure for the regulatory control period that is the same as that determined by the AER in a draft decision under rule 6A.12 to be a reasonable estimate of the provider's required capital expenditure for the regulatory control period; or
- (2) an amount of total forecast operating expenditure for the regulatory control period that is the same as that determined by the AER in a draft decision under rule 6A.12 to be a reasonable estimate of the provider's required operating expenditure for the regulatory control period,

then, except to the extent that:

(3) either or both of the following apply:

- (i) other changes have been made in the revised Revenue Proposal, by the provider; or
- (ii) the information contained in or accompanying the revised Revenue Proposal differs from that contained in or accompanying the previous Revenue Proposal; and

(4) the changes would justify the AER, in its final decision, in determining that the relevant amount is not a reasonable estimate of the provider's required operating expenditure or capital expenditure (as the case may be) for the regulatory control period, taking into account the matters referred to in clause 6A.6.6(b)(2) or 6A.6.7(b)(3), respectively,

the AER, in its final decision, must determine that those amounts are reasonable estimates.