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**Economic regulation of Transmission Services: The treatment of
forecast capital expenditure in the Draft-Revenue Rules**

Please find attached a copy of "The Group's" submission to the Commission's invitation for comments regarding the effect of the Draft-Revenue Rules in dealing with the treatment of forecast capital expenditure. "The Group" consists of:

- TRUenergy
- International Power
- Loy Yang Marketing Management Co.
- Flinders Power

Further information or clarification on this submission should be directed to Mr Con Noutso, Manager Regulation (Access), at TRUenergy on telephone (03) 8628-1240 or at con.noutso@trueenergy.com.au

Economic Regulation of Transmission Services

The treatment of forecast capital expenditure in the Draft-Revenue Rules

A. Introduction

The Commission has requested submissions from interested parties in relation to whether the National Electricity Rules “Rules” should provide that:

- A TNSP’s proposal must be accepted if the Australian Energy Regulator (AER) is satisfied that the forecast expenditure satisfies the criteria in the Rules; or
- The AER should have a residual discretion to substitute its own reasonable estimate of forecast expenditure in those circumstances

B. The Group’s position

The Group’s position on the Draft-Revenue Rule as it currently stands, given the legal advice provided by the Australian Government Solicitor, is that it has concerns with the current treatment of forecast capital expenditure.

Let me outline the key reasons why;

1. The current Rule proposal would force the AER to accept high capital expenditure forecasts submitted to the AER by a TNSP that were legally determined to be “reasonable” according to the criteria contained in the Rules. The capital expenditure forecasts that the AER would have to accept under this model would be higher compared with the results applied under the current regime. This conclusion is based on our understanding of the legal advice provided by the Australian Government Solicitor on this issue.
2. The proposed Rules should give the AER greater discretion in substituting a capital expenditure forecast for a regulatory period to allow it to determine a more accurate value of forecast capital expenditure. In the context of the propose-respond model, this means that the AER would be given greater discretion in refusing to accept a capital expenditure forecast submitted by a TNSP and allow the AER greater discretion to substitute a more accurate value of forecast capital expenditure.
3. The Group’s submission to the Chapter 6 Review supported the propose respond model. However, given the legal uncertainty attached to the term “reasonable” (Rule 6A 6.7) we specifically supported the AER’s suggestion to remove the requirement for the AER to accept a “reasonable estimate” as outlined in clause 6.2.6 (b) for capital expenditure, and require the AER to “have regard to” the remaining matters in clause 6.2.6(b) in making its

revenue determination. This would give the AER greater discretion in being able to substitute a capital expenditure forecast that it determined more accurately reflected a TNSP's capital expenditure requirements for a regulatory period, compared with the current Draft-Revenue Rule that forces the AER to accept a higher TNSP capital expenditure forecasts that would be legally determined to be "reasonable".

4. The Group notes that the Australian Government Solicitor's advice suggests that the formulation that required the AER to determine whether a total was a 'best estimate that is reasonably possible in the circumstances' would give the AER greater discretion to substitute a more appropriate value of capital expenditure when it was not satisfied with the value proposed by a TNSP. Whilst we have supported the AER's proposal that would give it greater discretion to substitute a better value of capital expenditure applied to forecasts, we would also support the Australian Govt's solicitor's proposal if it had the same effect.

C. Conclusion

So, in summary, the Group:

1. Remains concerned with the current treatment of forecast capital expenditure in the Draft-Revenue Rules especially if the current proposal forces the AER to accept high capital expenditure forecasts submitted to the AER by a TNSP that were legally determined to be "reasonable" .
2. Supports the Australian Energy Regulator's (AER) suggestion to remove the requirement for the AER to accept a "reasonable estimate" as outlined in clause 6.2.6 (b) for capital expenditure, and require the AER to "have regard to" the remaining matters in clause 6.2.6(b) in making its revenue determination giving the AER greater discretion to substitute a more accurate value of capital expenditure.
3. Alternatively supports the Australian Government Solicitor's advice to substitute the term "reasonable estimate" as outlined in clause 6.2.6 (b) for capital expenditure and require the AER to determine whether a total was a 'best estimate that is reasonably possible in the circumstances' giving the AER greater discretion to substitute a more accurate value of capital expenditure.