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20 October 2006

Dr John Tamblyn  
Chair  
Australian Energy Market Commission  
PO Box H166  
Australia Square NSW 1215

*5.4*  
Dear Dr Tamblyn

**RE: Draft Chapter 6 Rules – Forecast Capital and Operating Expenditure**

Please find attached the AER's submission in response to the AEMC's request for further submissions on the regime for the approval of forecast capital and operating expenditure set out in the Draft Rules.

Please contact me if you have any questions in relation to the matters raised in our submission.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Steve Edwell', written over a horizontal line.

Steve Edwell  
Chairman

### **Capex and opex forecasts: “Onus of proof” and “reasonable estimates”**

The AEMC has sought further comments on the regime for the approval of forecast opex and capex set out in the Draft Rules. The AER’s previous submissions on this issue have focussed on the potential uncertainty resulting from the use of a “reasonable estimate” criterion for the approval of opex and capex forecasts.

In its March 2006 submission in response to the AEMC’s Rule Proposal, the AER noted the finding of the Expert Panel that there is uncertainty surrounding the interpretation of “reasonable estimate”. The AER expressed the concern that this uncertainty has the potential to undermine consistency and predictability in regulatory outcomes. AGS has advised that while, under the Draft Rules, there will be a range of permissible estimates of forecast opex and capex, it is impossible to accurately predict how wide that range will be. The AER agrees with this advice.

The AEMC’s invitation for further comments is directed more towards whether there is an onus for establishing if a forecast is a reasonable estimate and the circumstances in which the AER can substitute its own estimate for that proposed by a TNSP. In relation to the questions identified by the AEMC, the AER makes the following comments.

#### **1. Do the Draft Rules impose an “onus of proof” on the TNSP or the AER?**

No. The AER agrees with the statements in paragraph 61 of the AGS advice dated 10 October 2006. The Draft Rules do not provide that the AER must accept a TNSP’s forecasts unless it *proves* they fail to satisfy the relevant provisions of the Rules. Rather, they state that the AER must accept a TNSP’s forecasts unless it *decides* they fail to satisfy the relevant provisions of the Rules. It remains a decision for the AER to be made having regard to the legislation and all other relevant matters.

#### **2. Is it necessary for the AER to form a view that a TNSP’s proposal is “unreasonable” before it could reject it?**

The Draft Rules provide that the AER must decide whether a TNSP’s forecast is a “reasonable estimate” of required expenditure having regard to a list of matters. The AER is of the view that it would be required to conclude that a TNSP’s forecast was not a reasonable estimate before it could reject that forecast.

#### **3. Do the Draft Rules operate to create a presumption in favour of acceptance of the TNSP’s proposed forecast expenditure if the AER was satisfied that the proposal met the criteria contained in the revenue rules?**

Yes. If the AER determines that a TNSP’s forecast is a reasonable estimate, it would be bound to accept that forecast for the purposes of a revenue cap determination.

**4. Should the Rules provide that:**

- (a) a TNSP's proposal must be accepted if the AER is satisfied that the proposal for forecast expenditure satisfies the criteria in the Rules; or**
- (b) the AER should have a residual discretion to substitute its own reasonable estimate of forecast expenditure in those circumstances?**

When a person submits an application that satisfies criteria prescribed in legislation, it typically follows that the relevant approval will be granted. It is unusual for a decision maker to retain some form of residual discretion to reject an application that satisfies the relevant legislative requirements.<sup>1</sup>

This does not mean the AER should be required to approve whatever is submitted by a TNSP. The Draft Rules provide that the AER must be satisfied that the TNSP's forecast is a reasonable estimate. As noted above, the AER has submitted that the Rules would be clearer if this criterion was removed.

That said, if, under the final Rules, the AER determines that a TNSP's forecast satisfies the criteria for approval (whether or not they include a "reasonable estimate" criterion) the AER does not believe it should have a residual discretion to reject the forecast. If this meant that the AER was required by the Rules to approve forecasts that are considered excessive, the AER believes the appropriate course of action would be to amend the Rules.

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<sup>1</sup> A similar issue, relating to authorisation under the Part VII of the *Trade Practices Act 1974*, is discussed in Heydon, *Trade Practices Law*, at paragraphs [1.460] to [1.490].