

IN THE MATTER OF ACTEWAGL DISTRIBUTION

ACTEWAGL DISTRIBUTION - AER DRAFT DECISION ON OPERATING EXPENDITURE FOR 2015 TO 2019 REGULATORY CONTROL PERIOD

MEMORANDUM OF ADVICE

EXECUTIVE SUMMARY

1. Our instructing solicitors act for ActewAGL Distribution (**ActewAGL**).
2. On 27 November 2014, the Australian Energy Regulator (**AER**) published its draft distribution determination for ActewAGL in respect of the 2014-19 regulatory control period (**Draft Decision**). In its Draft Decision, the AER concluded that it was not satisfied that the operating expenditure (**opex**) forecast in ActewAGL's Regulatory Proposal reasonably reflected the opex criteria specified in clause 6.5.6(c) of the National Electricity Rules (**NER**). Accordingly, the AER rejected ActewAGL's opex forecast and substituted its own opex forecast of \$220.3 million. The AER's Draft Decision represented a reduction in total opex of \$157 million (\$2013/14) from that proposed in ActewAGL's Regulatory Proposal (ie, a 41.7 per cent reduction).
3. We are instructed that were a similar decision to be made by the AER in the Final Decision, it would have a significant and deleterious impact on ActewAGL's ability to ensure the safe and reliable provision of network services.
4. ActewAGL has significant concerns about the manner in which the AER made its draft decision to reject ActewAGL's forecast opex and to determine an alternative forecast opex. Those concerns are expressed in ActewAGL's Revised Regulatory Proposal dated 20 January 2015.
5. ActewAGL's concerns appear to be well founded. In our view, the methodology that the AER has deployed to make its draft decisions about

forecast opex is inconsistent with the NER, in that it involves adopting the AER's own benchmarked reports as the primary reference point for making those decisions, and gives little or no weight to ActewAGL's forecast opex.

6. Further, in our view the AER has erred in making its Draft Decision, in that the AER has confined itself to the question of whether ActewAGL's forecast opex reasonably reflects the efficient costs of an objectively prudent provider, having regard only to exogenous considerations. The NER allows factors *endogenous* to ActewAGL to be taken into account in making decisions about forecast opex pursuant to clause 6.5.6(c) and 6.12.1(4)(ii) of the NER, where that is required to promote the national electricity objective in section 7 of the National Electricity Law (NEO and NEL respectively). In the particular circumstances of this case, the AER ought to have done so.
7. Finally, we have concluded that where the AER has determined that it would promote the NEO, it may be within the AER's discretion to allow a "glide path" pursuant to the control mechanism it has established pursuant to clause 6.12.1(11) of the NER so as to allow ActewAGL to transition its forecast opex to the opex that an objectively prudent provider might have incurred in ActewAGL's circumstances. However, there is a tension in this conclusion, in that it proceeds on the assumption that the NEO requires ActewAGL to be allowed forecast opex at a level which exceeds that which the AER has allowed to ActewAGL pursuant to clause 6.12.1(4)(ii) of the NER. In our view, it is difficult to imagine a circumstance in which that consequence might arise, without the AER's decision under clause 6.12.1(4)(ii) involving errors of the kind specified in section 71C of the NEL. Accordingly, the better view is that if ActewAGL requires forecast opex to, for example, ensure the safe and reliable supply of electricity, then that ought to be accommodated in the AER's decision pursuant to clause 6.12.1(4)(ii) of the NER, rather than by way of a "glide path".

BACKGROUND

8. Pursuant to Chapter 6 of the NER, the AER is required to make a distribution determination regulating the revenue that ActewAGL may earn over the regulatory control period commencing on 1 July 2014 and ending on 30 June

2019. That distribution determination is predicated on, among other things, constituent decisions concerning ActewAGL's forecast opex for that regulatory control period.¹
9. In November 2012, the Australian Energy Market (**AEMC**) introduced changes to the NER through its *Rule Determination, National Electricity Amendment (Economic Regulation of Network Service Providers) Rule 2012 (2012 Rule Determination)*. One of the changes introduced by the 2012 Rule Determination was to require the AER to undertake annual benchmarking reports for each distribution network service provider (**DNSP**), and to have regard to those reports when making distribution determinations.
 10. To allow for a transition to the new rules, the AEMC made transitional rules in Chapter 11 of the NER, which provided for two regulatory periods:
 - (a) a “transitional regulatory control period”, covering the period 1 July 2014 to 30 June 2015; and
 - (b) a “subsequent regulatory control period”, commencing on 1 July 2015 to the end of the regulatory control period.²
 11. On 16 April 2014, the AER made a placeholder distribution determination in respect of ActewAGL for the transitional regulatory control period.
 12. The AER is currently in the process of making a distribution determination for ActewAGL in respect of the subsequent regulatory control period. In making that distribution determination, the AER is required to determine a “notional” annual revenue requirement for the transitional regulatory control period,³ and then adjust the amount of the total revenue requirement for the subsequent regulatory control period by the difference between that notional amount and the amount that was approved for the transitional regulatory control period.⁴

¹ NER, clause 6.12.1(4).

² Division 2 of Part ZW of Chapter 11 of the NER.

³ NER, clause 11.65.4(c).

⁴ NER, clauses 11.65.4(h) and (i).

13. In its Regulatory Proposal for the subsequent regulatory control period, ActewAGL proposed total forecast standard control service opex of \$377.3 million (\$2013/14) for the 2014-19 period (excluding debt raising costs).
14. On 27 November 2014, the AER published its Draft Decision. The AER concluded that it was not satisfied that the opex forecast in ActewAGL's Regulatory Proposal reasonably reflected the opex criteria in clause 6.5.6(c) of the NER. In particular, the AER considered that ActewAGL's 2012/13 base year opex did not represent that which would be incurred by an objectively efficient and prudent service provider. Accordingly, the AER rejected ActewAGL's opex forecast and substituted its own forecast of total opex of \$220.3 million.
15. The AER's Draft Decision represents a reduction in total opex of \$157 million (\$2013/14) from that proposed by ActewAGL's regulatory proposal (ie, a 41.7 per cent reduction). By any measure, that reduction is momentous.
16. Further, the notional opex allowance in the AER's Draft Decision for the transitional regulatory control period is \$30.9 million lower than the amount allowed for that transitional regulatory control period. Accordingly, that difference is to be deducted from the annual revenue requirement for the subsequent regulatory control period pursuant to clauses 11.65.4(h) and (i) of the NER. The effect of this is that ActewAGL's total revenue requirement for the subsequent regulatory control period is even less than the amount that the AER considers to be reflective of an objectively prudent provider's efficient costs for that period.
17. In making that Draft Decision, the AER relied on a report by Economic Insights, which used a range of benchmarking methods to assess the relative opex efficiency of Australian DNSPs, including ActewAGL. The results of that report were deployed by the AER not only to make its decision to reject ActewAGL's forecast opex, but as a basis for calculating the substitute estimate of forecast opex for the base year.

18. In its Draft Decision, the AER explained the procedure it adopted in the following way:⁵

Our approach is to compare the service provider's total forecast opex with an alternative estimate that we develop ourselves. By doing this we form a view on whether we are satisfied that the service provider's proposed total forecast opex reasonably reflects the criteria. If we conclude the proposal does not reasonably reflect the opex criteria, we use our estimate as a substitute forecast.

...

Our estimate is unlikely to exactly match the service provider's forecast because the service provider may not adopt the same forecasting method. However, if the service provider's inputs and assumptions are reasonable, its method should produce a forecast consistent with our estimate.

If a service provider's total forecast opex is materially different to our estimate and there is no satisfactory explanation for this difference, we may form the view that the service provider's forecast does not reasonably reflect the opex criteria. Conversely, if our estimate demonstrates that the service provider's forecast reasonably reflects the expenditure criteria, we will accept the forecast.

19. ActewAGL has serious concerns about the effect of the AER's Draft Decision on its ability to recover revenue that is necessary to provide a safe, reliable and secure supply of electricity. In its Revised Regulatory Proposal, ActewAGL submits:⁶

The AER's draft decision reduces ActewAGL Distribution's opex to levels not seen since before 1999 and capex to levels last seen in 2007/08, despite an approximate 40 per cent increase in customer numbers, and close to a 40 per cent increase in new assets that now form part of ActewAGL Distribution's electricity network. These higher measures of output over the same period necessitate a higher level of opex and capex to provide a safe, reliable and secure supply of electricity.

AER'S USE OF ECONOMIC BENCHMARKING

Summary of conclusions

20. In our view, the manner in which the AER has deployed benchmarking reports to reject ActewAGL's forecast opex, and to decide an alternative forecast opex,

⁵ Draft Decision, page 7-12.

⁶ ActewAGL's Revised Regulatory Proposal, page v.

misconstrues the process that is prescribed by clauses 6.5.6 and 6.12.1 of the NER. Were those decisions to be made in the AER's Final Decision, therefore, they may be unlawful, in the sense that the AER is not empowered by the NER or the NEL to make those decisions.

21. Accordingly, in our view those decisions appear to give rise to one or more of the grounds of review specified in in section 71C of the NEL. In particular, we consider that the exercise of the AER's discretion appears to be incorrect, or the AER's decision unreasonable having regard to all the circumstances.⁷
22. If the AER's decisions are unlawful in the sense described above, it follows that they could not contribute to the achievement of the NEO, as required by section 16(1)(a) of the NEL, nor could those decisions be "preferable reviewable regulatory decisions" for the purposes of section 16(a)(d) of the NEL.

AER's decision places an onus on ActewAGL for purposes of clause 6.5.6(c) of the NER

23. The relevant legal and regulatory framework governing the manner in which the AER is make to make a constituent decision about ActewAGL's opex allowance is set out in detail in section 3.2 of ActewAGL's Revised Regulatory Proposal. We agree with the discussion contained within that section, and there is no need for us to repeat those matters in this memorandum.
24. We agree, in particular, that the NER mandates that a DNSP's proposal is the starting point for the AER's decision to determine its opex allowance. This is apparent from the terms of clause 6.5.6(c) of the NER itself, which provides that the AER must accept the relevant DNSP's forecast opex if it is satisfied that the total of the forecast opex for the regulatory control period reasonably reflects each of the operating expenditure criteria in clause 6.5.6 of the NER.

⁷ The Tribunal has held that a decision that is not determined by reference to the applicable criteria in the Law and the Rules is likely to have involved an incorrect discretion or would be unreasonable in all the circumstances: *Application by EnergyAustralia* [2009] A Compt 8 at [68]. The Tribunal noted that there was an overlap between the exercise of a discretion which is incorrect and a decision which is unreasonable.

25. Although the AER is required by clause 6.5.6(e)(4) of the NER to have regard to annual benchmarking reports in deciding whether to accept the DNSP's opex forecast, that is only one of a number of factors in clause 6.5.6(e) of the NER to which the AER must have regard. There is nothing in the NER to suggest that greater weight ought be placed on benchmarking reports than any other factor prescribed by clause 6.5.6(e) of the NER.
26. To the extent that the AER must have regard to benchmarking reports in making its decision under clause 6.5.6(c) of the NER, it is in the context of assessing the relevant DNSP's forecast opex within that DNSP's building block proposal.
27. This construction is consistent with relevant extrinsic material. In particular, the AEMC stated in its 2012 Rule Determination:

Benchmarking is but one tool the AER can utilise to assess NSPs' proposals. It is not a substitute for the role of the NSP's proposal. ...

The intention of a benchmarking assessment is not to normalise for every possible difference in networks. Rather, benchmarking provides a high level overview taking into account certain exogenous factors. It is then used as a comparative tool to inform assessments about the relative overall efficiency of proposed expenditure. This view is consistent with that put forward in a submission by Grid Australia to the consultation paper. Further, it is intended that the annual benchmarking report will be a useful tool for stakeholders, such as consumers, to engage in the regulatory process and have better information about relative performance of their NSPs.⁸

The NSP's proposal is necessarily the procedural starting point for the AER to determine a capex or opex allowance. The NSP has the most experience in how a network should be run, as well as holding all of the data on past performance of its network, and is therefore in the best position to make judgments about what expenditure will be required in the future. Indeed, the NSP's proposal will in most cases be the most significant input into the AER's decision.⁹

28. The AER's stated methodology, as described in paragraph 18 above, inverts the approach required by the NER. The AER's stated methodology involves using the AER's own forecast, derived from its benchmarking reports, as the starting premise for determining whether the DNSP's forecast reasonably reflects the opex criteria in clause 6.5.6(c) of the NER.

⁸ 2012 Rule Determination, page 107.

⁹ 2012 Rule Determination, page 111.

29. The AER has assumed, in particular, that “if the service provider's inputs and assumptions are reasonable, its method should produce a forecast consistent with our estimate”.¹⁰ That is to say, the AER has adopted, as a starting premise, the assumption that its own forecast is correct. That assumption appears to be confirmed by the following statement in the Draft Decision:¹¹

If a service provider's total forecast opex is materially different to our estimate and there is no satisfactory explanation for this difference, we may form the view that the service provider's forecast does not reasonably reflect the opex criteria.

30. Given that the most likely source of the “satisfactory explanation” as to the difference between the AER’s estimate and the DNSP’s estimate is the DNSP itself, the AER’s methodology appears to create an onus on the DNSP to provide that explanation. Further, in circumstances where the AER’s estimate has been (as we understand it) disclosed for the first time in the Draft Decision, ActewAGL has been placed in the position of only being able to commence seeking to discharge that onus *after* the Draft Decision was made, and in a limited time. In our view, the relevant provisions of the NER should not be construed in a way that permits such a result to occur.
31. As discussed above, the terms of clause 6.5.6 of the NER, as well as the statement by the AEMC referred to in paragraph 27 above to the effect that the DNSP’s proposal is “necessarily the procedural starting point” for determining forecast opex, is inconsistent with the AER’s methodology.
32. The AEMC itself eschewed the notion that there ought be any onus on any party (including the AER) in respect of the decision to accept or reject a DNSP’s opex forecast. In its 2012 Rule Determination, the AEMC states (bold emphasis added):¹²

The Commission remains of the view that the AER is not "at large" in being able to reject the NSP's proposal and replace it with its own. The obligation to accept a reasonable proposal, reflects the obligation that all public decision-makers have to base their decisions on sound reasoning and all relevant

¹⁰ Draft Decision, page 7-12.

¹¹ Draft Decision, page 7-12.

¹² 2012 Rule Determination, page 112.

information required to be taken into account. Some submissions have referred to the concept of an evidentiary burden, or onus of proof, as some submissions have termed it, that the AER has. To the extent the AER places probative value on the NSP's proposal, which is likely given the NSP's knowledge of its own network, then the AER should justify its conclusions by reference to it, in the same way it should regarding any other submission of probative value. **In circumstances where the NSP is required to provide information in support of its proposal, and the AER is required to explain its decision, an evidentiary burden does not appear to reside with one party more than another.**

33. In its Draft Decision, the AER concludes (bold emphasis added):¹³

We are not satisfied ActewAGL's total forecast opex reasonably reflects the opex criteria. **We compared ActewAGL's opex forecast to an opex forecast we constructed using the method outlined above. Our estimate is of the efficient opex a prudent operator would require to achieve the opex objectives. ActewAGL's proposal is higher than ours and we are satisfied that it does not reasonably reflect the opex criteria.** For this reason, we have substituted ActewAGL's total opex forecast with our total opex forecast.

34. The AER also states (bold emphasis added):¹⁴

We estimate an efficient service provider would need less base opex than a forecast based on ActewAGL's actual opex in 2012–13. Table illustrates how our efficient base level of opex compares with ActewAGL's actual opex in 2012–13. **We are satisfied our substitute base opex forms the appropriate starting point for total forecast opex that reasonably reflects the opex criteria.**

Table 7.4 Comparison of our estimate of base opex with ActewAGL's actual opex in 2012–13

	ActewAGL
Proposed base opex (adjusted) ^a	66.8
Substitute base opex	42.2
Difference	24.6
Percentage opex reduction	36.8%

¹³ Draft Decision, page 7-16.

¹⁴ Draft Decision, page 7-19.

35. Table 7.3 of the Draft Decision contains a summary of the techniques by which the AER has assessed ActewAGL's forecast opex. These techniques generally involve other forms of benchmarking, and are directed towards whether there was any explanation for the difference between benchmarked opex and ActewAGL's forecast opex, with the implicit assumption that if there was not an adequate explanation, the benchmarked opex reasonably reflected the opex criteria. Indeed, Table 7.3 contains the following entry:

Economic benchmarking	<p>Economic benchmarking measures the efficiency of a service provider in the use of its inputs to produce outputs.</p> <p>The economic benchmarking techniques we used to test ActewAGL's efficiency included Multilateral Total Factor Productivity, Multilateral Partial Factor Productivity and opex cost function modelling. We compared ActewAGL's efficiency to other service providers in the NEM.</p>	<p>Despite differences in the techniques we used, all benchmarking techniques show ActewAGL performs about half as efficiently as the most efficient service providers in the NEM (CitiPower and Powercor).</p> <p>We do not consider that differences in operating environment faced by ActewAGL adequately explain the different benchmarking results between ActewAGL and other service providers.</p>
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36. The AER appears to have conducted reviews of only two categories of expenditure: vegetation management and labour costs. However this analysis is limited, and appears to have been deployed by the AER, again, as a means of confirming that there is no adequate explanation for the differences between ActewAGL's forecast opex and the benchmarked results. For example, in relation to vegetation management, the AER states:¹⁵

While we accept backyard reticulation presents a unique challenge not seen in other networks, **we consider it only partially explains the gap in ActewAGL's performance compared to its peers.** We do, however, consider the incremental costs associated with backyard reticulation demonstrated by ActewAGL warrant an operating environment factor allowance because it may adversely affect ActewAGL's benchmarking results. [emphasis added]

¹⁵

Draft Decision, page 7-32.

37. That is to say, the AER has adopted, as its starting position, the benchmarked results, and assessed ActewAGL's forecast against that, rather than assessing ActewAGL's forecast opex against the range of opex factors prescribed by clause 6.5.6(e) of the NER (including annual benchmarking reports).
38. The implicit onus that the AER's methodology places on ActewAGL is, in our view, contrary to manner in which clause 6.5.6(c) of the NER contemplates a decision to accept or reject a DNSPS's forecast opex will be made. That error is more than a mere matter of form. As discussed above, it creates an onus on ActewAGL that it can only begin to discharge after the Draft Decision is made. Such a decision would not, therefore, be authorised by the NER. The exercise of the discretion in that way would either be incorrect, or unreasonable, within the meaning of sub-sections 71C(1)(c) or (d) of the NEL. Further, a decision which does not conform with clause 6.5.6(c) cannot, in our view, be regarded as a decision that contributes to the NEO, as required by section 16(1)(a) of the NEL, nor could that decision be a "preferable reviewable regulatory decision" for the purposes of section 16(a)(d) of the NEL.

Unreasonable to place primary reliance on benchmarking for purposes of clause 6.5.6(c)

AER approach elides a proper consideration of opex factors in clause 6.5.6(e)

39. Although clause 6.5.6(e)(4) of the NER requires the AER to consider each of the factors prescribed in that sub-section (ie, the "opex factors") in making a decision under clause 6.5.6(c), the AER is not required to give each of those considerations equal weight. It may consider some of those factors irrelevant, or not equally probative.
40. However, we agree with the submission made by ActewAGL in its Revised Regulatory Proposal that the AER's discretion in that regard is not unlimited, and must be exercised reasonably.¹⁶ Having regard to the matters raised in section 3.4.4.3 of ActewAGL's Revised Regulatory Proposal, the primacy

¹⁶ ActewAGL's Revised Regulatory Proposal, page 90.

given to benchmarking in the AER's draft decision to reject ActewAGL's proposed opex appears to be inconsistent with the primary value of benchmarking, which is to serve as a tool to identify significant areas of expenditure anomaly between businesses which are then subject to further detailed investigation. The submissions made by ActewAGL about the limitations of benchmarking in its Revised Regulatory Proposal further confirm the undesirability of using benchmarking in a deterministic way.¹⁷

41. We note the observations made in ActewAGL's Revised Regulatory Proposal that the AER's opex draft decision is inconsistent with and undermines the service quality incentive framework (**STPIS**). Clause 6.5.6(e)(8) of the NER provides that the AER must have regard to whether an operating expenditure forecast is consistent with any incentive scheme that applies to the DNSP.
42. The AER's stated methodology of using its own forecast, derived from its benchmarking reports, as the starting premise for determining whether the DNSP's forecast reasonably reflects the opex criteria in clause 6.5.6(c), is inimical to a proper consideration of clause 6.5.6(e)(8) of the NER, or, indeed, any of the other factors prescribed by clause 6.5.6(e) of the NER. The AER's methodology appears to assume that its own forecast, derived from benchmarked results, is consistent with all the opex factors, without giving proper and discrete regard to each of them.
43. To the extent that there is a discrepancy between the benchmarked results and ActewAGL's forecast opex, the Draft Decision does not disclose that significant further investigation has occurred, having regard to the opex factors. Rather, as discussed above, the AER has largely assumed that, absent an adequate explanation for that discrepancy, ActewAGL's forecast opex should be rejected.
44. Of itself, the magnitude of the reduction of forecast opex that the benchmarked results indicate should occur, ought to have caused the AER to have extensive regard to all of the factors prescribed by clause 6.5.6(e) of the NER. This is particularly so in a context where, on our instructions, the benchmarked results

¹⁷ ActewAGL's Revised Regulatory Proposal, pages 131 to 133.

depart significantly from opex allowed in previous distribution determinations, and where there is no suggestion in the Draft Decision that those decisions were incorrectly made. That fact, of itself, suggests that the results of benchmarking reports ought to have been treated with considerable caution, rather than being used as the starting premise for the AER's conclusions.

45. In the circumstances, by adopting an approach of placing primary importance on benchmarked results, the AER appears to have acted unreasonably, by failing to have proper regard to the factors prescribed by clause 6.5.6(e) of the NER. The AER's draft decision to reject ActewAGL's forecast opex does not, therefore, appear to contribute to the NEO, nor does it appear to be a preferable reviewable regulatory decision.

AER approach elides a proper consideration of opex criteria in clause 6.5.6(c)

46. The AER's stated methodology also elides a proper consideration of the "opex criteria" in clause 6.5.6(c) of the NER.
47. Clause 6.5.6(c) of the NER requires that ActewAGL's forecast opex "reasonably reflects" *each* of the following:
- (1) the efficient costs of achieving the opex objectives (ie, the objectives specified in clause 6.5.6(a) of the NER);
 - (2) the costs that a prudent operator would require to achieve the opex objectives; and
 - (3) a realistic expectation of the demand forecast and cost inputs required to achieve the opex objectives.
48. Clause 6.5.6(c) of the NER requires that each criterion be addressed by the AER, in order that it may be "satisfied" that a DNSP's opex forecast reasonably reflects each of them. Further, it is clear that, for the purposes of considering what the efficient costs of a DNSP might be, the inquiry is to be undertaken in a context where a DNSP might be required to make business decisions that are not governed by cost considerations, but are governed by wider considerations reflective of the need to secure safety and reliability of supply.

49. Likewise, the requirement in clause 6.6.5(c)(3) that consideration be given to “a realistic expectation of the demand forecast and cost inputs required to achieve the opex objectives” is different to the requirement in clause 6.6.5(c)(1) that consideration be given to “efficient costs”. The difference between the two may reflect the fact that in the particular circumstances of a DNSP, costs inputs might be required to deliver the opex objectives that are different to those which an objectively efficient DNSP would otherwise incur.
50. We note, in this context, that the discussion of the relationship between “efficiency” and “prudence” in the NERA Report cited in *Application by Energy Australia* [2009] A Compt 8 at [142] suggests that an assessment of prudence can be expected to lead to satisfaction of the efficient costs criterion “over time”. The discussion of this issue in the NERA Report is somewhat opaque, but, at the very least, it suggests that “efficient costs” might have a meaning, including as to its temporal dimensions, that is affected by what a DNSP would regard to be prudent.
51. Nevertheless, the Draft Decision appears to be predicated on the assumption that the opex criteria are identical, or that they can be conflated into a single criterion. At page 7-10, the Draft Decision states:

We assess the proposed total forecast opex against the opex criteria set out in the NER. The opex criteria provide that the total forecast must reasonably reflect:

1. the efficient costs of achieving the operating expenditure objectives
2. the costs that a prudent operator would require to achieve the operating expenditure objectives
3. a realistic expectation of the demand forecast and cost inputs required to achieve the operating expenditure objectives.

The AEMC noted that '[t]hese criteria broadly reflect the NEO [National Electricity Objective]’.

52. At page 7-12, the Draft Decision states:

Underlying our approach are two general assumptions:

1. the efficiency criterion and the prudence criterion in the NER are complementary

2. actual expenditure was sufficient to achieve the expenditure objectives in the past.
53. Despite these statements, the analysis in the Draft Decision of ActewAGL's opex forecast, as described earlier in this memorandum, does not disclose that the AER has had regard to each of the opex criteria separately. Rather, the AER appears to have assumed, for the purposes of its analysis, that each of the opex criteria in sub-clause 6.5.6(c)(1)-(3) of the NER can be conflated into a single criterion of productive efficiency.
 54. This "rolling up" of the three criteria by the AER is evidenced in a number of statements in the Draft Decision which use the phrase "efficient" and "prudent" as if they were identical, without seeking to draw a distinction between the two or to assess the extent to which they are interrelated in the context of ActewAGL's forecast opex.¹⁸
 55. Further, by adopting the methodology described in paragraph 18 above of assessing ActewAGL's total forecast opex against an alternative estimate that the AER developed itself principally in reliance on benchmarking reports, the AER has effectively sidestepped discrete and focussed consideration on whether each opex criterion has been met. Rather, the AER has adopted, as a starting premise, the assumption that benchmarked results properly reflect each of the opex criteria, unless the DNSP establishes otherwise.
 56. In our view, the AER's failure to give discrete consideration to each opex criterion, and the assumption that a forecast derived from benchmarked results will satisfy the opex criteria, involves a misapplication of the process mandated by clause 6.5.6(c) of the NER by which ActewAGL's forecast opex was to be considered. Accordingly, were the AER to adopt the same approach in the Final Decision, in our view its decision might be regarded as involving an exercise of discretion in a way that is either incorrect, or unreasonable, within the meaning

¹⁸ See in particular pages 7-50 and 7-51 of the Draft Decision, in which the AER states, for example, "our assessment is necessarily focussed on forecasting what an objective efficient and prudent service provider would require to achieve those opex objectives" and "[I]f our determined prudent and efficient allowance to achieve the opex objectives is lower than actual past expenditure, our view is that a prudent operator would take the necessary action to improve its efficiency".

of sub-sections 71C(1)(c) or (d) of the NEL. Further, its decision could not be regarded as a decision that contributes to the NEO, as required by section 16(1)(a) of the NEL, nor could that decision be a “preferable reviewable regulatory decision” for the purposes of section 16(a)(d) of the NEL.

Unreasonable to place primary reliance on benchmarking for purposes of clause 6.12.1(4)

57. Where, acting in accordance with clause 6.5.6(c) of the NER, the AER rejects a DNSP’s forecast opex, the AER is required by clause 6.12.1(4)(ii) of the NER to estimate that DNSP’s required opex for the relevant regulatory control period that the AER is satisfied reasonably reflects the opex criteria, taking into account the opex factors.
58. In the Draft Decision, the AER arrived at a substitute base opex for ActewAGL pursuant to clause 6.12.1(4)(ii) of the NER by starting with Economic Insights’ Cobb Douglas Stochastic Frontier Analysis (SFA) model. That model would, without adjustment, have seen a reduction in ActewAGL’s base year opex of 61%.¹⁹
59. The AER then made three adjustments to the “raw” benchmarking results:²⁰
- (1) first, rather than using the National Energy Market (**NEM**) frontier service provider, CitiPower, as the benchmark for efficiency comparisons, the first adjustment was to set a lower benchmark based on an average of the efficiency scores of the most efficient service providers in the NEM;
 - (2) secondly, the AER modified the benchmark efficiency target to account for operating environment factors specific to the ACT. The AER was satisfied that a 30 per cent operating environment adjustment would be appropriate for ActewAGL; and

¹⁹ Draft Decision, page 7-27.

²⁰ Draft Decision, page 7-27.

- (3) thirdly, the AER applied a trend to move the substitute base opex from a forecast of the average amount for the 2006 to 2013 period to a forecast for 2012–13, the base year.

60. Table A.3 to the Draft Decision summarises the basis on which the AER made its decision:

Starting point: 'Raw' CD SFA forecast with frontier service provider as benchmark	26.0
Adjustment 1: Change benchmark to weighted average of top quartile efficiency score range	+ 2.7
Adjustment 2: Adjust benchmark to account for operating environment factors	+ 8.6
Adjustment 3: Adjust benchmark to move from average results to 2013 results	+ 4.9
Substitute base opex	42.2

61. By adopting this methodology, the AER appears to have disregarded ActewAGL's forecast opex, and has instead relied on its own forecast opex, which has been almost entirely derived from benchmarked results.
62. As discussed above, the AEMC contemplated that when exercising its discretions pursuant to clauses 6.5.6(c)-(d) and 6.12.1(4) of the NER, "the AER is not 'at large' in being able to reject the DNSP's proposal and replace it with its own." The AEMC observed that:

To the extent the AER places probative value on the NSP's proposal, which is likely given the NSP's knowledge of its own network, then the AER should justify its conclusions by reference to it, in the same way it should regarding any other submission of probative value.

63. Indeed, it is implicit in the opex factors prescribed by clause 6.5.6(e) of the NER, to which the AER is obliged to have regard by 6.12.1(4) of the NER, that the AER must have regard to the DNSP's forecast opex when determining a substitute opex. That is evident from the repeated use of the phrase "operating

expenditure forecast”, which plainly refers to the DSNP’s forecast, not the AER’s alternative forecast.

64. There is nothing in the Draft Decision to suggest that the AER considered that ActewAGL’s forecast opex, and the reasons advanced in support of it, had no probative weight. Accordingly, the AER ought to have had regard to that forecast opex, and to the extent that the AER determined to depart from it, advanced reasons for doing so.
65. That was particularly important in a context where, as discussed above, the benchmarked results departed so markedly not only from ActewAGL’s forecast opex, but the results of the AER’s own previous determinations, which the AER has not concluded were incorrectly decided.
66. These problems are compounded because, as discussed in paragraphs 46 to 56 above, in deciding to adopt its own forecast opex, the AER has not discretely considered the opex criteria in clause 6.5.6(c) of the NER. Rather, the AER appears to have assumed that the benchmarked results, as modified, necessarily satisfy each of those three criteria.
67. The question of whether, as a matter of fact, ActewAGL’s forecast opex is consistent with the opex criteria depends on a range of technical and financial information that we have not reviewed, and which we cannot express an opinion about. Likewise, although we note that serious technical deficiencies have been asserted in ActewAGL’s Revised Regulatory Proposal about the benchmarking reports deployed by the AER, an assessment of the merits of those assertions is beyond the scope of this advice. However, the errors we have set out above about the methodology used by the AER to assess ActewAGL’s forecast opex appear, in our view, to be sufficient to establish one or more of the grounds of error in sub-sections 71C(1)(c) and/or (d) of the NEL.

AER’S FAILURE TO HAVE REGARD TO ENDOGENOUS FACTORS

68. The AER has made a further error in its Draft Decision. In its Draft Decision, the AER limited its consideration to the question of whether the forecast opex

reasonably reflected the costs of an objectively prudent provider, rather than a provider in the particular circumstances of ActewAGL. That approach was adopted despite the fact that, if the assertions made in ActewAGL's Revised Regulatory Proposal are accepted, a reduction in its opex to the level determined by the AER in its Draft Decision may have a catastrophic impact on ActewAGL's ability to deliver safe and reliable supplies of electricity. This consequence may arise from ActewAGL's inability to make a sudden alteration to its business structure to accommodate the significant reduction in opex that the Draft Decision would require it to achieve, particularly in a context where the reduction in opex has retrospective effect. In our view, the AER was in error not to consider that issue when making its determinations under clause 6.5.6(c) and 6.12.1(4) of the NER.

69. As our instructing solicitors will be aware, prior to the 2012 Rule Determination, clause 6.5.6(c)(2) of the NER required the AER to consider whether the forecast opex for the regulatory control period reasonably reflects the costs that a prudent operator "in the circumstances of the relevant Distribution Network Service Provider" would require to achieve the opex objectives.
70. In its 2012 Rule Determination, the AEMC discussed the rule change in the following terms:

The Commission is of the view that the removal of the "individual circumstances" clause does not enable the AER to disregard the circumstances of a NSP in making a decision on capex and opex allowances. Benchmarking is but one tool the AER can utilise to assess NSPs' proposals. It is not a substitute for the role of the NSP's proposal. Should the phrase remain, it appears that the AER's interpretation of it may restrict it from utilising appropriate benchmarking approaches to inform its decision making.

The Commission considers that the removal of the "individual circumstances" phrase will clarify the ability of the AER to undertake benchmarking. It assists the AER to determine if a NSP's proposal reflects the prudent and efficient costs of meeting the objectives. That necessarily requires a consideration of the NSP's circumstances as detailed in its regulatory proposal.

Under the first expenditure criterion the AER is required to accept the forecast if it reasonably reflects the efficient costs of achieving the opex objectives. These include references to the costs to meet demand, comply with applicable obligations, and maintain quality, reliability and security of supply of services and of the system. These necessarily require an assessment of the individual

circumstances of the business in meeting these objectives. So to the extent that different businesses have higher standards, different topographies or climates, for example, these provisions lead the AER to consider a NSP's individual circumstances in making a decision on its efficient costs.

71. The 2012 Rule Determination also states (bold emphasis added):

The final rule gives the AER discretion as to how and when it undertakes benchmarking in its decision-making. However, when undertaking a benchmarking exercise, circumstances exogenous to a NSP should generally be taken into account, and endogenous circumstances should **generally** not be considered. In respect of each NSP, the AER must exercise its judgement as to the circumstances which should or should not be included. However exogenous factors to be taken into account are likely to include:

- geographic factors: topography and climate;
- customer factors: density of the customer base (urban v rural), load profile, mix of customers between industrial and domestic;
- network factors: age, mix of underground and overhead lines, though this will depend on the extent to which this is at the election of the NSP; and
- jurisdictional factors: reliability and service standards.

If there are some exogenous factors that the AER has difficulty taking adequate account of when undertaking benchmarking, then the use to which it puts the results and the weight it attaches the results can reflect the confidence it has in the robustness of its analysis.

Endogenous factors not to be taken into account may include:

- the nature of ownership of the NSP;
- quality of management; and
- financial decisions.

72. These passages suggest that, “generally”, in exercising its discretions pursuant to clauses 6.5.6(c) and 6.12.1(4) of the NER, the AER is not to have regard to opex that is required to be incurred by reason of structural inefficiencies that were caused by the DNSP’s own business decisions. The AER observes, in its Draft Decision, that ordinarily it would expect a service provider (including its shareholders) to wear the cost of any inefficiency, rather than consumers.²¹

²¹ Draft Decision, page 7-16.

73. In its Draft Decision, the AER concludes:²²

We must be satisfied that the opex forecast reasonably reflects the efficient costs of a prudent operator (not the service provider in question), given reasonable expectations of demand and cost inputs, to achieve the opex objectives.

It is important to note the effect of a change to the NER in November 2012 on this point. Previously, the NER provided that the total forecast opex should reasonably reflect the costs that a prudent operator *in the circumstances of the service provider* would require to achieve the objectives. The reference to "in the circumstances of the service provider" was deleted from this rule to ensure that the opex forecast would reasonably reflect the costs of an objectively prudent provider, rather than a provider in the particular circumstances of the service provider concerned.

74. We agree that, generally speaking, it may be consistent with the NEO to limit a DNSP to the efficient costs that a hypothetical DNSP in its position in a workably contestable market would incur to achieve the opex criteria, leaving aside, for the moment, what is meant by the phrase "efficient", and provided that proper account is taken of the opex criteria and opex objectives. As the AER observes in the Draft Decision, the scheme contemplated by the NER creates incentives, in that if a service provider spends inefficiently or imprudently, it will bear those additional costs and, conversely, if it achieves efficiencies it may make additional profits. This reflects conditions that would be faced by businesses operating in a competitive environment.²³

75. However, the passage from the Draft Decision set out in paragraph 73 above overstates the reasons for the rule change. The 2012 Rule Determination does not exclude the possibility that it may, in appropriate circumstances, be necessary to have regard to the endogenous circumstances of a DNSP for the purposes of making a determination under clauses 6.5.6(c) and 6.12.1(4) of the NER.

76. Section 7 of the NEL defines the NEO in the following terms:

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—

²² Draft Decision, page 7-49.

²³ Draft Decision, page 7-49.

- (a) price, quality, safety, reliability and security of supply of electricity; and
 - (b) the reliability, safety and security of the national electricity system.
- 77. Section 16 of the NEL provides that the AER must, in performing or exercising an AER economic regulatory function or power, perform or exercise that function or power in a manner that will or is likely to contribute to the achievement of the NEO referred to in section 7 of the NEL.
- 78. The application of clauses 6.5.6 and 6.12.1(4)(ii) of the NER necessarily involves discretionary considerations. Further, clause 6.12.3 of the NER makes it clear that the AER has a discretion to accept or approve any element of a regulatory proposal:

Subject to this clause and other provisions of this Chapter 6 explicitly negating or limiting the AER's discretion, the AER has a discretion to accept or approve, or to refuse to accept or approve, any element of a regulatory proposal.
- 79. Although clause 6.12.3 is expressed in binary terms, that is, a discretion to “accept or approve, or to refuse to accept or approve” an element of a regulatory proposal, in our view the discretion granted by clause 6.12.3 extends to a decision pursuant to clause 6.12.1(4)(ii) of the NER to determine the level of substitute forecast opex that the AER will allow (or “approve”).
- 80. In those circumstances, it is not only consistent with the scheme of the NEL and the NER, but also relevant extrinsic material, for the AER to have regard to relevant endogenous factors in exercising its discretions under clauses 6.5.6 and 6.12.1(4)(ii) where that is necessary to promote the NEO. Indeed, in our view the AER is obliged to do so.
- 81. ActewAGL’s Revised Regulatory Proposal states:

The AER’s draft decision reduces ActewAGL Distribution’s opex to levels not seen since before 1999 and capex to levels last seen in 2007/08, despite an approximate 40 per cent increase in customer numbers, and close to a 40 per cent increase in new assets that now form part of ActewAGL Distribution’s electricity network. These higher measures of output over the same period necessitate a higher level of opex and capex to provide a safe, reliable and secure supply of electricity.

ActewAGL Distribution contends that the AER's expenditure allowances, if reflected in the AER's final decision, will deliver a short-term reduction in prices at the cost of a significant compromise to the long term interests of consumers with respect to reliability, security and safety.

82. ActewAGL's Revised Regulatory Proposal also states:²⁴

To work within approved expenditure allowances, ActewAGL Distribution would have to quickly adopt a fundamentally different business model: a "care and maintenance model". This means that current activities would be scaled back to the provision of essential business activities only, which are required to maintain network reliability and public safety.

Operating such a business model is expected to have significant impacts on ActewAGL Distribution's current service levels, reliability and safety.

83. These consequences, if they were to occur, would not be consistent with the NEO. Further, those consequences arise in a context where, as discussed previously, the AER has approved levels of opex in excess of those it has approved in the Draft Decision, which the AER has not asserted were incorrectly decided, and in circumstances where ActewAGL has, not unreasonably, structured its business to accommodate opex at those approved levels.
84. Further support for the conclusion that the AER has a discretion to consider endogenous factors in making decisions about the levels of opex that it approves, where it is appropriate to do so, is to be found in the use of the words "reasonably reflects" in clause 6.5.6(c). In its 2012 Rule Determination, the AEMC indicated that the term "reasonable" in this context is to accommodate the lack of precision in the exercise of setting opex, which means that there will be a certain margin of difference between the AER's forecast and that of the DNSP, within which the AER could say that the DNSP's forecast is reasonable. The AEMC stated, "[w]hat the margin is in a particular case, and therefore what the AER will accept as reasonable, is a matter for the AER exercising its regulatory judgment."²⁵

²⁴ Revised Regulatory Proposal, page 68.

²⁵ 2012 Rule Determination

85. Although the observations of the AEMC were directed towards a lack of precision in determining opex, in our view, the phrase “reasonable” allows the AER to exercise a more general discretion where it would promote the NEO to do so. Thus, in considering whether an opex forecast “reasonably” reflects the opex criteria, there is scope for the AER to allow opex at a level in excess of the efficient costs which an objectively prudent DNSP might incur.
86. This is particularly the case where, as ActewAGL points out in its Revised Regulatory Proposal, citing NERA, 2014, *Economic Interpretation of Clauses 6.5.6 and 6.5.7 of the NER*:²⁶
- It is therefore unrealistic to expect a firm to always be operating on the efficiency frontier. Even if a firm is on the efficiency frontier at one point in time, it is unlikely also to be on it a moment later, as the frontier itself will have moved. In practical terms, efficiency is something that firms may be constantly working towards, without ever actually achieving.
87. In all of these circumstances, it would in our view be unreasonable for the AER not to consider the individual circumstances of the DNSP, and make allowance for those circumstances, where it would promote the NEO to do so. That is to say, it would not be consistent with the NEO for the AER to presume, from the outset, that its discretion is circumscribed so that it must *only* consider the efficient costs that an objectively prudent DNSP might incur.
88. In particular, the AER has an obligation to consider the manner in which ActewAGL has structured its business in reliance on previous determinations made by the AER, and its ability to transition to much lower levels of opex immediately.
89. We note, in this context, that the AER made the following observations in the Draft Decision:²⁷

If our determined prudent and efficient allowance to achieve the opex objectives is lower than actual past expenditure, our view is that a prudent operator would take the necessary action to improve its efficiency. This view seems to be supported by AGL, who submitted that in competitive markets, prudent and efficient firms incur short term costs to increase efficiency because

²⁶ Revised Regulatory Proposal, page 49.

²⁷ Draft Decision, page 7-51.

the benefits of those costs will accrue to the owners in the long-term. On the information before us, our view is, mirroring what would be expected under competitive market conditions, it would be appropriate for service providers (including their shareholders) to bear the cost of any inefficiency rather than consumers.

90. In the ordinary course of events, such a statement might be regarded to be unexceptional. However, it assumes that the DNSP is operating in the context of a series of distribution determinations that were correctly decided, and that the DNSP has had an opportunity to adjust its business to reflect the costs that a prudent DNSP might have incurred in a competitive market. Indeed, the references in the extrinsic material discussed above about endogenous considerations “generally” being irrelevant implicitly assume that the DNSP is operating in a regime in which it has, or will have had, the opportunity to adapt its business to approach the efficiency frontier.
91. However, the magnitude of the reduction in opex determined by the AER in its Draft Decision, its retrospective effect, its sudden impact, and the submissions made by ActewAGL about the effect of the Draft Decision on its ability to ensure the safety and reliability of its services, suggest that the AER’s decision, were it to be implemented, would be an extraordinary event to which the observations made by the AER in paragraph 89 above are inapposite. The magnitude of the reduction in opex contemplated by the AER, and the circumstances in which it would be imposed on ActewAGL, would not be such that ActewAGL could simply adjust its short terms costs to increase efficiency. ActewAGL submits that it would have to swiftly make a dramatic change to its business model simply to meet a reduction in revenue, which may preclude it from expending resources on initiatives that would have longer term efficiency benefits.
92. In the circumstances, the AER not only has power to consider endogenous factors particular to ActewAGL in making its decisions under clause 6.5.6 and 6.12.1(4)(ii) of the NER, but in our view is required to do so. The AER is not permitted by the NER and the NEL to presumptively inhibit its discretion by adopting an ex-ante limitation that it must only consider whether the opex forecast reasonably reflects the costs of an objectively prudent provider. The

AER must also, in our view, give consideration to whether subjective matters particular to the DNSP ought be taken into account, where it is necessary to do so to promote the NEO.

93. The AER must also, in the context of considering the impact on an individual DNSP of its decisions, have regard to the long-term dynamic efficiency of that DNSP (ie, the ability of that DNSP to make changes to its business to generate longer term productive efficiencies). The AER ought not simply consider the short-term productive efficiency of the DNSP. To do so would be inimical to the NEO, which is directed to the long-term interests of consumers.
94. The Draft Decision does not disclose that any of these endogenous and long-term considerations were taken into account by the AER. In the particular circumstances of this case, therefore, were the AER to adopt the same approach in its Final Decision, it will have made one or more of the errors specified in section 71C of the NEL.

ESTABLISHMENT OF A GLIDE PATH

95. As discussed above, in our view, the AER has a discretion (and, indeed, an obligation) to consider whether to allow forecast opex in excess of the short term productively efficient costs an objectively prudent DNSP might incur. However, where the AER decided that it would promote the NEO to allow those additional costs, the AER might have a discretion about the mechanism by which it will do so.
96. The first alternative is to allow those costs in the DNSP's forecast opex pursuant to decisions made under clauses 6.5.6 and 6.12.1(4)(ii) of the NER. As discussed above, the AER has a discretion to allow opex referable to endogenous factors in the particular circumstances of the DNSP concerned. Thus, where it would promote the NEO to do so, the AER may allow costs in excess of the costs that an objectively efficient DNSP might incur, to allow the DNSP to restructure its business structure in an orderly way, in anticipation that future distribution determinations might allow lower levels of opex. Were this mechanism to be adopted, there would not be a formal "glide path" to lower

levels of opex; rather, it would be implicit in the distribution determination that opex was being allowed at a higher level than might be incurred in later regulatory control periods, because of transitional issues that it may not be appropriate to take into account in those future regulatory control periods.

97. The second alternative is to allow a “glide path” towards the efficient costs an objectively prudent provider might incur pursuant to the AER’s decision about a control mechanism under clause 6.12.1(11) of the NER. That is to say, the AER might elect, pursuant to its decision under clause 6.12.1(4)(ii) of the NER, to allow forecast opex at a level that does not have regard to endogenous considerations, while at the same time allowing for the relevant DNSP to recover a higher level of opex through the control mechanism. This would allow the DNSP to transition to that forecast opex over time.
98. The provisions of the NER that are relevant to the establishment of a “glide path” include the following:
 - (a) Clause 6.2.5(a) of the NER provides that a distribution determination is to impose controls over the prices of direct control services, the revenue to be derived from direct control services, or both.
 - (b) Clause 6.2.6 of the NER provides that for standard control services, the control mechanism must be of the prospective CPI minus X form, or some incentive-based variant of the prospective CPI minus X form, in accordance with Part C.
 - (c) Clause 6.5.9 of the NER provides that if the control mechanism relates generally to standard control services – the X factor must be designed to equalise (in terms of net present value) the revenue to be earned by the Distribution Network Service Provider from the provision of standard control services over the regulatory control period with the provider's total revenue requirement for the regulatory control period.
99. These clauses do not, however, suggest that the AER’s discretion to determine a control mechanism is limited in a way that would preclude the AER from making allowance for additional elements, beyond the X factor, that might

permit a DNSP to earn revenue in excess of its total revenue requirement for the regulatory control period, where it would be in the NEO to do so. Indeed, the reference to “incentive-based variant of the prospective CPI minus X form” appears to be an express contemplation that the ultimate form of the control mechanism might not equalise a DNSP’s revenue and total revenue requirement for the regulatory control period.

100. Clause 6.12.1(11) of the Rules requires the AER to include in ActewAGL's distribution determination for the subsequent regulatory control period a decision on the form of the control mechanism (including the X factor) for standard control services and on the formulae that give effect to that control mechanism.
101. Clause 6.12.3(c1) of the Rules provides that the formulae that give effect to the control mechanisms must be as set out in the relevant framework and approach paper unless the AER considers that unforeseen circumstances justify departing from the formulae as set out in the paper.
102. In its Framework and Position Paper for ActewAGL dated March 2013, the AER stated that it proposed to apply the following formula for standard control services, to give effect to a revenue cap:²⁸

$$(1) MAAR_t \geq \frac{\left(\sum_{i=1}^n \sum_{j=1}^m p_{ij}^t q_{ij}^{t-2} \right)}{kWhtransported_{t-2}}$$

$$(2) MAAR_t = AAR_t + \frac{(I_t + T_t + B_t)}{kWhtransported_{t^*}}$$

$$(3) AAR_t = AAR_{t-1}(1 + CPI_t)(1 - X_t)$$

103. T_t is defined as the sum of transitional adjustment in year t , which is “to be decided in the final decision”.²⁹

²⁸ Framework and Position Paper ActewAGL dated March 2013, page 38.

²⁹ Framework and Position Paper for ActewAGL dated March 2013, page 38.

104. It does not appear from the position paper that the term T_t is intended to encapsulate adjustments to ActewAGL's total revenue requirement under clause 11.56.4(h) of the NER. However, we agree with the observations on pages 259 to 260 of ActewAGL's Revised Regulatory Proposal that the definition of the term T_t is broad enough to permit transitional adjustments to allow a glide path, even if that were to have the result of allowing ActewAGL opex in excess of the opex allowed pursuant to the AER's decisions under clauses 6.5.6 and 6.12.1(4)(ii) of the NER.
105. Although we think that the establishment of a "glide path" is open to the AER, having regard to the analysis above, there is a tension in this conclusion, in that it proceeds on the assumption that the NEO requires ActewAGL to be allowed forecast opex at a level which exceeds that which the AER has legitimately allowed to ActewAGL pursuant to clause 6.12.1(4)(ii) of the NER. In our view, it is difficult to imagine a circumstance in which that consequence might arise, without the AER's decision under clause 6.12.1(4)(ii) involving errors of the kind specified in section 71C of the NEL. Accordingly, the better view is that if ActewAGL requires particular levels of forecast opex to, for example, ensure the safe and reliable supply of electricity, that ought to be accommodated in the AER's decision pursuant to clause 6.12.1(4)(ii) of the NER, rather than by way of the control mechanism.

13 February 2015



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