

Independent Expert Report
nbn SAU Variation Expenditure

DRAFT

24 April 2023

Final draft

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Part D Recommendations

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1 Part D summary

- Findings taken from the expenditure assessment carried out and described in this Report as well as (brief) comparisons to other jurisdictions and the role the AER takes are used to recommend a process that seeks to build on the existing IOP and SAU Variation processes adopted by NBN Co.
- An Annual Reporting and ACCC Review process is recommended to support ex post assessment of expenditure at the end of the regulatory cycle and ex ante assessment of expenditure proposed for the next regulatory cycle.
- Tools recommended to support the recommended Annual Reporting and ACCC Review process are:
 - o Annual reporting template (leveraging existing data and information NBN Co has provided to ACCC as part of the assessment described in Part C of this Report),
 - o Benefit framework to articulate targeted benefits and track benefits realisation during the regulatory period (with a focus on LTIE),
 - o Mechanism for change to allow NBN Co to update the ACCC with any material changes at any point mid-cycle during the financial year, and within the regulatory cycle, and
 - o Pre-defined business case requirements to support any new or significant changes to forecast expenditure initiatives. (It is strongly recommended that NBN Co and ACCC adopt a pre-agreed business case process for proposed expenditure items moving forward to assist with expenditure assessments).
- Armed with the pre-existing data and information and the tools recommended for the Annual Reporting and ACCC Review process, ACCC and NBN Co will be supported in establishing and running a robust, comprehensive and adaptable framework for monitoring, reporting and eventual assessment of expenditure from a prudency and efficiency perspective.

2 Context

Further to the SAU Variation and assessment carried out between late December and the release of this draft Report described in Parts A to C of this Report, this Part D set outs a recommended process for assessment of expenditure by ACCC and NBN Co, to commence during the First Regulatory Cycle.

The recommended process seeks to build on the existing IOP and SAU Variation processes carried out by NBN Co to develop a robust, comprehensive and adaptable framework for monitoring and reporting purposes. The recommended process seeks to enable ACCC monitoring and review of the progress of NBN Co's forecast expenditure on an annual basis, as well as to compare results with forecasted estimates from the previous forecasted period based on tangible information supported by pre-defined key metrics that provide insight and justify the measurable benefit value that the relevant proposed NBN Co expenditure item is seeking to provide.

The goal of this process is to provide the ACCC with three years' worth of consistent, reliable and measurable data on NBN Co's performance and outcomes in line with estimated forecasts and funding, and to allow the ACCC to use this historical data to make informed decisions and monitor NBN Co's activities accurately.

This process in turn provides the ACCC with information that helps inform the next regulatory cycle.

Outside of the delivery to ACCC of the tools and data to support its decision-making process, the recommended process should also be of benefit to NBN Co in the following ways:

- Allows NBN Co to make a case for proposed new or amended expenditure, and to outline proposed targeted benefits for an expenditure item/initiative and how NBN Co expects to achieve these targeted benefits,
- Provides both NBN Co and the ACCC with ongoing information on how current initiatives are tracking, and whether these initiatives are on time and within forecasts,
- Provides NBN Co with a tool for demonstrating clear and measurable benefit value of its initiatives and provides RSPs and the public with clear definitive uses of government-funded programs,
- Enables NBN Co to prepare for the ex post and ex ante process at the end of the three-year review cycle, and
- Allows NBN Co to notify ACCC of change outside of the Annual Review cycle.

As a final explanatory note, the recommendations made in this section are underpinned by the key assumptions that the new process does not impact NBN Co's business as usual activities, and that the new process does not provide unnecessary information or conflict with previously provided information.

3 Recommended expenditure review process for the First Regulatory Cycle

Using the findings from the assessment described in Part C of this Report, the recommended process seeks to leverage the data and information already in existence through NBN Co's current processes and proposed approach in the SAU Variation. However, the recommendations in this Part C are intended to:

- gather key insights,
- avoid gaps in information,
- provide templates that are easy to complete, and
- introduce a discrete process for cost-benefit analysis.

The new process will allow the ACCC to make informed changes to the next regulatory review cycle, by improving accountability and tracking the delivery of proposed projects and initiatives, all of which will assist ACCC's review of expenditure from a prudence and efficiency perspective.

The outcomes of the process are to provide:

- **NBN Co** with a simple, holistic tool to:
 - o deliver and explain further tangible information representing key metrics and costs,
 - o elaborate on the proposed benefits that are an outcome of proposed and forecast expenditure, and
 - o deliver a business case to justify the cost-benefit of proposed expenditure items.
- **ACCC** with renewed (modified) annual reports, that:
 - o monitor, track and record data and information to support its assessments,
 - o highlight the benefit metrics laid out by NBN Co's current initiatives, and
 - o measure historical progress across the regulatory cycle.

A new reporting and monitoring process is recommended that includes a new data collection tool and a supporting framework, namely the **Annual Reporting Template**, and the **Benefit Framework**. Together, these provide NBN Co and ACCC with a simple, intuitive, and holistic reporting method that links planned initiatives with benefit outcomes (further described in section 3.6 below).

3.1 Overview

The below illustration of the recommended regulatory monitoring, review and assessment process is further described in the following subsections for the individual components of the recommended process.

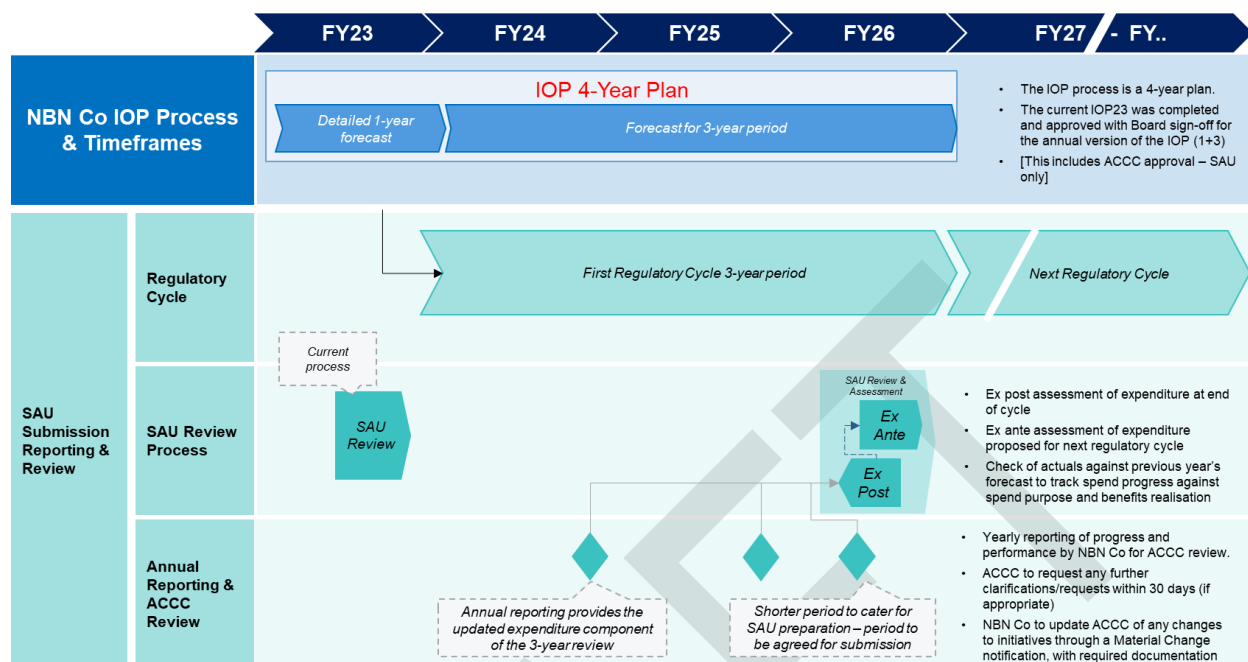


Figure 1 Recommended process to prepare for and review expenditure (Source: Grex)

3.2 “NBN Co IOP Process & Timeframes”

The IOP Process is an internal NBN Co process, comprising of a 4-year (‘1+3’ year) plan that refreshes every year with renewed forecasts. It is a pre-determined process that has existed in NBN Co for a number of years.

The current iteration, ‘IOP23’ was completed and approved with NBN Co Board sign-off for the annual version of the IOP process.

This includes capex and opex forecasts for its expenditure initiatives for the next three years i.e., FY24-FY26 (see Figure 1 above), aligned with the timeline for the First Regulatory Cycle. At the end of the FRC, the ex ante process will assess the original forecasts provided by IOP23, against the actuals provided by NBN Co (annually) throughout the FRC to create a comparison between actuals and original forecasts wherever practicable.

3.3 “Regulatory Cycle”

This swimlane in the illustration is used to contextualise where the recommended Annual Reporting & ACCC Review would take place.

The First Regulatory Cycle (FRC) will start from FY24, run for a period of three years, and end at the end of FY26, when the ex ante expenditure review process will be completed. The information received through the NBN Co IOP Process for the FRC is recommended to feed through to the SAU Review Process and the Annual Reporting & ACCC Review.

3.4 “SAU Review Process”

The SAU Review Process described in this phase follows the existing SAU process as defined/recommended by the SAU Variation and the regulatory framework.

The expenditure assessment carried out in this Report falls under the current process of review of the SAU Variation being carried out by ACCC. This SAU Review takes place before the commencement of the First Regulatory Cycle on 1 July 2023, with a review and assessment carried out in FY26 (i.e., the final year of the FRC).

The recommended future SAU Review and assessment is carried out in two forms, the ex post and the ex ante process, and can be summarised as follows:

- Ex post assessment of expenditure at the end of the regulatory cycle, and
- Ex ante assessment of expenditure proposed for the next regulatory cycle.

The ex post and ex ante reviews and assessments are to be executed simultaneously, however, the ex post review will start just before the ex ante process, so the end results of the ex post will feed into the decision-making process of the ex ante review and assessment.

The “Annual Reporting and ACCC Review” is intended to feed three years of historical and tracking data into the SAU Review and Assessment process.

The ex post and the ex ante processes are recommended to have a suitable timeframe to conduct a review in the final year of the FRC, and would require NBN Co and the ACCC to finalise the duration of the review period.

It is recommended that NBN Co will continue to provide actuals data leading up to the ex post and ex ante processes (up until the review begins), and provide a forecast for the remaining months of the financial year i.e., FY26 for the FRC. The format would include ‘x’ months of actuals followed by ‘y’ months of forecasts (‘x+y’ process).

Ex Post Review

The ex post review process is a two-part process, beginning with a final annual submission from NBN Co, followed by a review process from the ACCC.

The review will look at the accumulated historical data (actuals), and compare it to NBN Co's original capex forecasts from the IOP Process provided at the start of the FRC. The review will assess whether NBN Co delivered on their forecasted targets and provide this assessment to the ex ante process i.e., the decision making process.

NBN Co will provide a summary of its progress, goals and hurdles over the three year regulatory period, with a rationale for outcomes linked to any changes in spend or impacts on forecasts. This will include a summary of the remaining regulatory period and any justifications for final actuals varying from the original forecasts.

NBN Co is also presented with an opportunity to provide ACCC with any recommendations moving forward. ACCC in turn will use this information in the ex ante process to support its own decisions and recommendations moving forward, before a final decision is made.

Ex Ante Review

The ex ante review process can be defined in two parts; a decision-making process based on the result of the ex post review, and a regulatory review process that informs or proposes requirements for the next regulatory cycle moving forward.

This process is also recommended to begin at a suitable timeframe before the end of the regulatory cycle, to allow sufficient time for decisions to be made by ACCC in conjunction with NBN Co that may shape and inform the next regulatory cycle.

The decision-making process is based on the ex post review, tracking spend progress against spend purpose and benefits realisation i.e., 'Prudent and Efficient' assessment of the forecasted and actual capex over the three year regulatory period (overspend/underspend assessment).

This will also include an assessment of forecasted expenditure proposed for the next regulatory cycle. The ex ante submission will include any updates required for existing reporting processes.

3.5 Annual Review

3.5.1 “Annual Reporting & ACCC Review”

It is recommended that an Annual Reporting & ACCC Review framework is established to support a robust, comprehensive and adaptable reporting and monitoring process.

As this is an annual process within the FRC, there will be two iterations of this Annual Reporting and ACCC Review, which will be completed at the end of the financial year i.e., FY24 and FY25.

For the third financial year of the First Regulatory Cycle, this reporting period will be brought forward to accommodate the a period of actuals and a period of forecasts for the remainder of the financial year, with the results feeding into the ex post review; and will include

The results of the actuals provided create a clear and comparable value based on the IOP forecasts submitted at the start of the regulatory cycle and renewed annually.

Where there are clear differences between forecasts and actuals post NBN Co's annual submission (of actuals for the previous year), the ACCC can ask for any further clarifications or requests for information, including a justification as to why this is the case. The ACCC can do so through a Request for Information (RFI) process, only if the appropriate information was not provided.

The ACCC will have to engage the RFI process with NBN Co within 30 days from NBN Co's submission. This is designed to prevent the development of an overly tedious and onerous process.

Outside of the Annual Review period, should NBN Co be required to update the ACCC of any significant changes to its initiatives, NBN Co can do so through an official Material Change notification process, which will require updated forecasts, supporting documentation and a clear and well-defined business case where required.

The ARR achieves this through the new data collection tools as defined in the following section.

The outcome of this process is a submission from NBN Co and a review from the ACCC. This forms a transparent process and does not anticipate or require the ACCC to intervene or approve NBN Co's submission.

As explained in section 3.4, the ex post process under the SAU Review Process will both review the existing capital expenditure and inform the ex ante process of any changes to initiatives/expenditure items. It is only during the ex ante process that the ACCC makes a decision.

3.6 New tools and framework to support assessment

It is recommended that new data collection tools and frameworks are established by ACCC and NBN Co to support the recommended process of ex ante and ex post review and assessment.

3.6.1 Annual reporting template

An “Annual Reporting Template” is recommended to be designed as a simple and intuitive tool to provide clear linkages between benefit and performance improvement, and service levels.

It is recommended that NBN Co develop a reusable template for regular reporting with the ACCC and use it to provide the ACCC with actuals for the previous time period i.e., financial year, or the remaining months prior to the ex post and ex ante process.

The template would build off existing capital and operating expenditure categories (metrics) that have been previously provided by NBN Co to the ACCC through the process undertaken to prepare this Report as well as other previously established processes. The template would also include additional metrics and further levels of detail that have previously not been provided or required on a yearly basis.

Where information (items/unit costs) has not been previously provided, NBN Co will complete the template by filling in missing values. It is not expected that NBN Co would require any significant work to be done to complete this template, as these metrics would already be available at NBN Co through its own internal processes.

The template should include (as a minimum):

- Volume, unit, cost & performance (benefit targets and realisation) metrics, and
- A mechanism for change (to notify the ACCC).

The purpose of compiling the new, more comprehensive metrics, are:

- to create tangible costs that can provide insight and links to real and tangible benefits,
- to provide further layers of detail on the drivers of expenditure (aimed at assisting an expenditure review by ACCC),
- to add further layers of accountability and responsibility, and
- for the Benefit Framework to provide these metrics with a link back to the total costs proposed by NBN Co for their rollout initiatives.

Through the development of a formal and more diligent annual reporting process, the aim is to create an environment for NBN Co to prepare for the ex post and ex ante process because the same structures and reporting process would be required for the SAU Review. NBN Co would therefore be preparing for the ex post review far ahead of time due to the annual reporting process, while providing the ACCC with actuals for the three year regulatory period.

The implementation of an annual review process would also provide the ACCC with historical data leading up to the ex post process (approx. 2.5 years into the FRC), rather than being provided with three years of actuals at the end of the FRC.

3.6.2 Benefit framework

A “Benefit Framework” is recommended to be established and used in conjunction with the Annual Reporting Template to assess individual initiatives for the impact each initiative has on the network or end-user (including LTIE) and the viability of each initiative (cost/benefit). It will allow NBN Co to closely align their projected spend to direct and indirect benefits, justifying their metrics and costs previously provided to the ACCC.

The benefit realisation metrics derived from the Benefit Framework would be incorporated into the Annual Reporting Template, with an illustrative guide to benefit realisation provided in Figure 2 below:

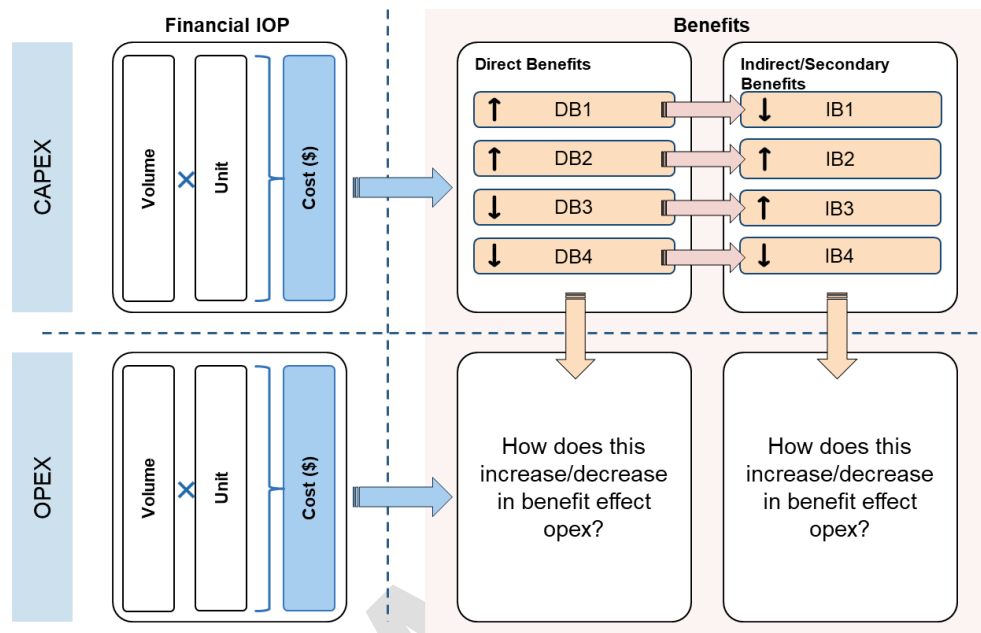


Figure 2: Illustrative example of how the Benefit Framework links both capex and opex metrics with direct and indirect benefit realisation.

With support from the Benefit Framework, the annual reporting template will provide a link across detailed metrics for defined capex and opex expenditure categories, and subcategories, which will include:

- Expenditure forecast,
- Volume forecast,
- Unit forecast, and
- Performance forecast.
- Benefit forecast
- Direct benefits, and
- Indirect (secondary) benefits.

The Benefit Framework will close the gap between expenditure set aside to achieve each initiative, and the resulting benefit obtained from pursuing the respective initiative, i.e., the link between cost and benefit. This will form a strong basis for any business case presented by NBN Co to the ACCC and has been defined and explained in detail in Section 3.7.

3.6.3 Mechanism for Change

To allow for unforeseen circumstances or any changes to initiatives outside the Annual Review timeline, NBN Co will be provided with a mechanism for change. This will allow NBN Co to update the ACCC with any material changes at any point mid-cycle during the financial year, and within the regulatory cycle.

Any changes to existing NBN Co initiatives or for the addition of new initiatives, will require NBN Co to notify the ACCC.

Upon internal approval of the change, NBN Co will notify the ACCC of the following, or provide the following:

- any material changes,
- any changes to the forecasted budget,
- submit supporting documents, and
- provide a business case (in accordance with the requirements of the process for the form and content of a business case).

Key uses for this change mechanism are listed below:

- for initiatives that are no longer relevant/valid,
- to include new initiatives or change to initiatives, and/or
- to be conducted with the discretion of the ACCC.

3.7 Business case requirements

A business case is a document that outlines the justification for a proposed project or initiative from a business perspective. It presents a detailed analysis of the costs and benefits of the project, including financial, operational, and strategic considerations. The purpose of a business case is to help decision-makers determine whether or not to proceed with the project by providing a comprehensive evaluation of the risks and rewards associated with it.

There are many different types of business cases depending on the organisation in question. However, items that are generally present across any type of organisation include:

- **Business need:** clear rationale for investment which addresses a need based on an identified priority, outcome and business case objective,
- **Options or responses:** long-list options that could be utilised to address the business need (including “doing nothing”),
- **Cost-benefit analysis:** analysis of benefits against costs to obtain a Benefit Cost Ratio (BCR), which is used to analyse and rank prospective options,
- **Financial analysis:** to determine financial feasibility and affordability of the options,
- **Commercial analysis:** to determine whether the options/solutions can be procured, supplied and maintained at the service level proposed, and
- **Management analysis:** to confirm that the solution put forward is deliverable, and that governance and systems are in place to optimise value and be modified if required in response to ongoing monitoring and evaluation.

Whilst the 6 basic components summarised above are common across generic business cases, government organisations and those seeking government funding are often subject to far more rigorous business case requirements. The diagram below illustrates the high-level requirements of an NSW Treasury business case across the initial 3 stages.

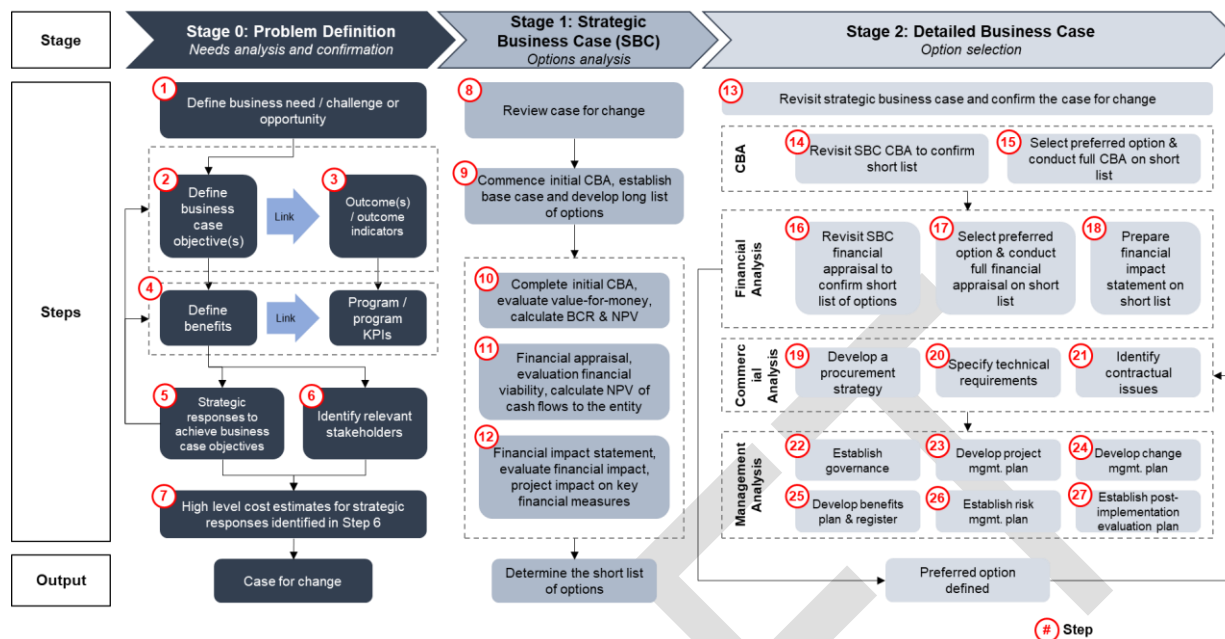


Figure 3 NSW Treasury Business Case Requirements¹

It is strongly recommended that NBN Co develop business cases for expenditure items proposed, working with ACCC to develop a pre-agreed framework for the business case, including any practicable templates. As outlined above, there are multiple examples of this used in similarly regulated environments.

¹ NSW Treasury – TPP18-06 NSW Government Business Case Guidelines

4 Record Keeping Rule

As an adjunct to and complementary with the above recommended process, the ACCC is proposing to develop a new record keeping rule (RKR) to collect service quality and network performance information from NBN Co and in the future other superfast broadband network providers.

The focus of the record keeping rule is to collect service quality and network performance information to assist the ACCC in identifying service issues affecting broadband customers and providing greater transparency through public reporting of this information.

This initiative follows several recent ACCC review and consultation processes that raised issues regarding the transparency of NBN Co's service quality and network performance and that of Superfast Broadband Access Service (SBAS) providers. The need for greater transparency and better reporting relating to NBN Co's service quality has been identified by stakeholders through these processes.

The intent behind the RKR and associated public reporting is to increase the transparency of service quality and network performance by NBN Co and in the future that of Superfast Broadband Access Service (SBAS) providers. As described, the RKR is being designed to enable future benchmarking of service performance across networks and identification of systemic issues regarding service quality.

Several aspects of service quality and network performance, have been outlined, and related service level metrics and data are proposed to be collected through an RKR, namely:

- connections,
- faults including service dropouts and recurring faults,
- appointments,
- network outages,
- network performance including speed capability,
- services attracting NBN Co rebates when service levels are not met, and
- corrective action taken by NBN Co to ensure its performance objectives are met.

The proposed benefits of a monitoring and reporting framework applying across NBN Co and other large scale wholesale broadband networks, and future public reporting, are intended to complement operational reporting between NBN Co and RSPs under wholesale access agreements and NBN Co's Special Access Undertaking (SAU). Also, greater public transparency of NBN Co service quality, along with improved operational reporting between NBN Co and retailers, is intended to improve outcomes for end users over time and reduce overall costs relating to the management of faults and outages, among other things. Factors such as the quality of a retailer's network and its direct interactions with end users will also impact on service levels and the quality of service experienced by end users.

The ACCC intends to also collect and report on information relating to the service quality and network performance of SBAS providers in the future.

The reporting of the service quality and network performance metrics and related service level metrics as part of the RKR framework can also support the case for measuring the overall benefits delivered by NBN Co's programs and the related expenditure. Mapping the service quality and

performance metrics of the RKR framework to the value and benefits delivered by the program initiatives will identify the delivery of an improved end-user experience (e.g., improved service performance, willingness to pay, customer service assurance). This may require the addition of new/improved service metrics to the RKR framework that align to NBN Co's programs and initiatives; seeking to measure and monitor value indicators for the delivery of benefits for the end-user service experience.

The associated RKR service metrics would quantify the benefits/outcomes and indicate trends over time and would seek to ensure the business case outcomes and benefits articulated and identified through the process recommended in this Part D are measured along with the monitoring of expenditure and budget adherence that NBN Co carries out presently.

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5 Other jurisdictions

5.1 UK, Canada and New Zealand

For the purposes of a (brief) comparison of the above recommended process to other jurisdictions, the table below provides a summary comparison of the expenditure-related monitoring methods and levels of public and private information disclosure required in the comparable jurisdictions of UK, Canada and NZ.

A significant amount expenditure-related detail is presented to regulators by operators which could be compared to NBN Co in UK and NZ. For example, Chorus is required to produce a document similar in nature to NBN Co's Initial Cost Allocation Manual, which describes the methodology regarding cost allocation. Chorus's documentation consists of 248 pages of detailed cost allocation inputs, methodology, and outputs across opex only.² NBN Co's equivalent document proposes to provide only its methodology, which is documented in 14 pages across both capex and opex.³

² Commerce Commission, 2023, https://comcom.govt.nz/__data/assets/pdf_file/0033/253599/Analysys-Mason-report-for-Chorus-Documentation-of-opex-allocation-for-the-BBM-Opex-workstream-including-responses-to-notice-to-supply-information-Model-version-3-31-22-March-2021.pdf

³ NBN Co, 2022, nbn initial Cost Allocation Manual

Comparison	ACCC	UK Ofcom	Canada CRTC	NZ ComCom
Equivalent Regulated Entity	NBN Co	Openreach (owned by BT)	Various wholesale providers	Chorus
Regulation	SAU	Wholesale Fixed Telecoms Market Review 2021-2026	CRTC Regulatory Framework	Price Quality & Information Disclosure
Regulatory Reporting & Frequency	LTRCM Annual –	Regulatory Financial Statements – Annual	Canadian wholesale broadband providers are not required to report expenditure-specific information to the regulator or publicly (outside of financial reporting and accounting requirements). Instead, CRTC’s regulatory framework focuses primarily on the provision of access to wholesale broadband services to internet service providers (ISPs) on a non-discriminatory basis, and on ensuring that wholesale broadband rates are fair and reasonable through facilities-based competition regulation, specified access rates and terms & conditions, set wholesale rates, and disaggregated wholesale high-speed access service (new)	PQ, ID-Only, and ID reports – information on network management must be disclosed annually, no later than 5 months after the end of a disclosure year
Information Required for Public Disclosure	<ul style="list-style-type: none"> - LTRCM - BBM including RAB & ABBRR 	<p>For Markets with Significant Market Power (SMP Markets):</p> <ul style="list-style-type: none"> - Revenue, volumes, price, opex, capex (mean capital employed and return on capital employed) - Market-specific information requirements such as operating costs and mean capital employed across granular components (e.g., lead-in ducts) 		<p>Among significant other levels of Price Quality (including RAB) and Information Disclosure requirements, Chorus must disclose information regarding asset and network management, including:</p> <ul style="list-style-type: none"> - Self-assessment report on asset management capability - Explanation on the link between historical and forecast capex and: forecast opex; and

Comparison	ACCC	UK Ofcom	Canada CRTC	NZ ComCom
		<p>internal and external operating costs and MCE)</p> <ul style="list-style-type: none"> - RAB Model for Area 3 		<p>network quality performance</p> <ul style="list-style-type: none"> - Opex and capex based on standardised formats and categories - Information about the network - Information about forecast capacity and utilisation and demand
<p>Information Required for Private Disclosure to Regulator</p>	<p>As above, with commercially sensitive information included</p>	<ul style="list-style-type: none"> - Data and models supporting the RFS (directly from CostPerform - BT's cost allocation software) - A breakdown of costs attributed using previously allocated costs (PAC) methodologies - A mapping between the operating cost and MCE of each cost component and the operating cost and MCE cost categories from the market performance summary 		<ul style="list-style-type: none"> - Expenditure and supporting information forecast for years 4-5 - Forecasts of assets to be replaced in next five years - ID-only asset register - Active forecast connections by service level - Forecast demand by POI area - Connection numbers

Comparison	ACCC	UK Ofcom	Canada CRTC	NZ ComCom
		<ul style="list-style-type: none"> - A breakdown of grant funding and associated expenditure by asset category - Other market-specific information for a number of SMP Markets 		

Table 1: Comparison of Monitoring Across UK, Canada & NZ

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6 Australian Energy Regulator (AER)

6.1.1 Overview

For a further comparison with and context for the above recommended process, this section provides a brief summary of the role the Australian Energy Regulator (AER) takes in monitoring and reviewing the energy sector within Australia across the following markets:

- Wholesale energy market,
- Energy networks, and
- Retail energy market.

Regulating the wholesale energy market, the AER monitors, investigates, and enforces compliance with national energy legislation and rules within the wholesale electricity and gas markets in Australia. They release reports referencing prices outside regular thresholds, as well as quarterly reports on compliance monitoring activities⁴.

The AER sets maximum amounts of revenue that electricity and networks and natural gas pipelines can earn in order to regulate the markets. Network businesses submit their proposals to the AER on the revenues required, which are reviewed by the AER before making a final decision.

The AER regulates electricity and gas markets in jurisdictions that have commenced the National Energy Retail Law, while they do not set retail energy prices, the AER provides a price comparison website to aid customers in finding the best energy offers for their needs. The AER still monitor and enforce compliance with obligations in the Retail Law, Rules and Regulations, despite not setting prices.

The NER regulatory expenditure factors have been drawn on by NBN Co with a high degree of alignment. The NER expenditure factors are split by topic⁵:

- Past expenditure and relevant benchmarks
- Alignment with end-users, access seekers and consumer advocacy groups, and with current and reasonably anticipated future market conditions
- Expenditure Justification
- Procurement and governance
- Financing expenditure
- Balance between opex and capex
- Other matters

6.1.2 AER Collection of Information and Determination Process

As part of its role in setting maximum revenue, the AER collects information from regulated businesses in order to undertake its functions. The AER uses Regulatory Information Notices

⁴ Australian Energy Regulator, 2023, <https://www.aer.gov.au/about-us/our-role>

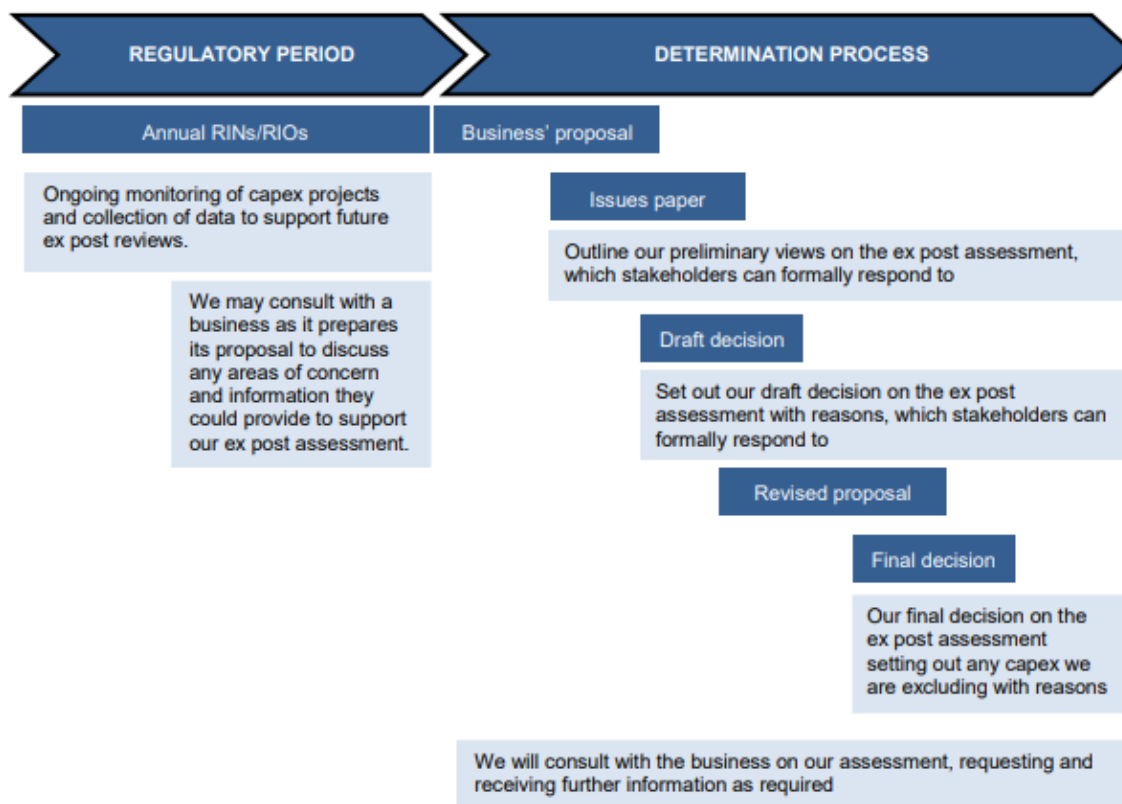
⁵ nbn Special Access Undertaking Variation 2022 – Supporting submission Part F: Efficiency of nbn's Expenditure and Demand Forecasts pg.14

(RIN) to collect information, at the time it is making a regulatory determination about that business and annually throughout the regulatory period. The AER publishes non-confidential information received from regulated businesses in order to support effective and transparent regulatory process and ensure that stakeholders can access information on issues affecting their interests.⁶

The information required for disclosure under AER RINs can vary depending on the specific RIN issues, but typically includes:

- **Assets & Network:** details about the energy company's operations and assets, such as generation capacity and location, demand, network reliability, network integrity.
- **Financial Information:** revenue, income, capex & opex (generally by asset class/opex category & purpose of expenditure), related party transactions, provisions, pass-throughs, and assets (asset base).
- **Volumes:** Information about the energy company's volume-related metrics, including the number of customers and the types of services provided.
- **Compliance Information:** such as whether the energy company is meeting regulatory requirements.

The RINs are collected and monitored annually, and input into the revenue determination process which is generally every 5 years. The figure below illustrates how the ex post review of annual RINs/RIOs (Regulatory Information Order) aligns to the determination process.



⁶ Australian Energy Regulator, 2023, <https://www.aer.gov.au/networks-pipelines/performance-reporting/jemena-gas-networks-nsw-gas-pipeline-information-rin-responses>

Figure 4: RIO & ex post Review Alignment to Determination Process⁷

6.1.3 AER Expenditure Forecast Assessment Guideline for Electricity Distribution

The AER practices a three stage assessment process to assess whether a Network Service Provider (NSP) is prudent and efficient across their expenditure forecasts. The three stages include a first pass or initial decision, followed by detailed assessments to provide a draft decision, with a final decision to follow.

The AER practices several General Assessment Techniques to assess the Distribution Network Service Provider's (DNSP) expenditure forecasts during the AER's ex ante process. The following Table 2, highlights four of the eight General Assessment Techniques that are relevant to the ACCC's regulatory process.

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⁷ AER, 2022, Draft Capital Expenditure Incentive Guideline for Electricity Network Service Providers

General Assessment Techniques	AER assessment guideline	AER detailed explanation/need	Relevance to the ACCC's regulatory process
Cost Benefit Analysis (CBA)	Assessing whether the business has chosen spending options that reflect the best value for money	A cost benefit analysis is required to highlight the option with the highest net benefit, with the lowest life cycle costs when compared with other projects on an equivalent basis. Therefore, a cost benefit analysis requires optionality and net benefit analysis.	Using the new recommended process and templates, NBN Co and the ACCC can conduct detailed Cost Benefit Analysis to highlight initiatives that provide the highest net benefit with the lowest capex and opex costs across a time-period.
Project Review	A detailed engineering examination of specific proposed projects or programs	A detailed project review on large expenditure (non-recurrent) projects require business cases along with other information. Detailed reviews also assess whether the timing of the project is efficient, and whether volume, and unit costs meet relative benchmarks.	The AER project review require business cases to assess whether the DNSP practice good governance in developing each project. Mandating the need for business cases where required, would be crucial for the assessment of NBN Co's initiatives on the practice of good governance, by the ACCC. The ACCC's detailed review would also include performance levels.
Methodology Review	Examining processes, assumptions, input and models that the business used to develop its proposal	The AER will assess whether the NSP's methodology is reasonable, based on AER criteria. DNSPs are expected to not only provide forecasts, but also provide their models, assumptions and inputs, to prove that their projects are prudent and efficient.	A methodology review would provide a clear understanding of how NBN Co develops and justifies their initiatives. The ACCC can assess the NBN Co's methodology based on pre-defined criteria such as those laid out in the SAU.

Governance & Policy Review	Examining the business's strategic planning, management, asset and prioritisation	AER will use governance reviews as a holistic assessment of DNSP's internal processes compared with industry best practice. A governance review may indicate a DNSP's likely overall efficiency and areas for further analysis.	Governance and Policy review includes a risk management assessment. The ACCC can conduct its own risk management assessment during the ex ante process, or request NBN Co to provide their own risk assessment for the ACCC to review.
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Table 2: Relevant General Assessment Techniques practiced by the AER (Source: Grex Analysis, AER^{8,9,10})

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⁸ AER Better Regulation factsheet – expenditure forecast assessment guideline
⁹ AER Expenditure forecast assessment guideline - Electricity distribution - August 2022
¹⁰ AER Expenditure Forecast Assessment Guideline - Explanatory Statement

The AER has specific and detailed information requirements for Capex categories that vary from the Opex categories, and are required to be provided by the DNSPs to support the required assessment (see Figure 5 below).

CAPEX Category Specific Information	OPEX Category Specific Information
Replacement <ul style="list-style-type: none"> Assets added and disposed Average value, age of assets Expected costs of replacing assets Data justifying historic and forecast replacement activities. 	Maintenance <ul style="list-style-type: none"> Routine maintenance Non-routine maintenance Supporting data to explain volume
Augmentation <ul style="list-style-type: none"> Demand forecast including data such as peak demand, probability of exceeding 10% and 50% of forecast Actual forecast models and input to the model Specific data on augmentation such as capacity constraints, unit cost, etc, including network segment specific data 	Emergency <ul style="list-style-type: none"> Weather events Other events Supporting data to explain volume
Connection <ul style="list-style-type: none"> Forecast volumes Forecast costs 	Vegetation mgmt <ul style="list-style-type: none"> Tree trimming, inspection and audit Supporting data
Non-Network <ul style="list-style-type: none"> Forecast volumes Forecast costs 	Network Overheads <ul style="list-style-type: none"> How are these reported in other Capex/Opex Network mgmt. Network monitoring & control Network system operation Supporting data on scale and cost
	Corporate Overheads <ul style="list-style-type: none"> How are these reported in other Capex/Opex categories Human resources, CEO, legal etc Workload etc

Figure 5: Capex and Opex category specifications as laid out by the AER (Source: Grex Analysis, AER^{11,12,13})

The recommended regulatory review process moving forward could build on the above takeaways from AER's Expenditure Forecast Assessment Guidelines, as described in Table 2, and Figure 5, with the following learnings listed below:

- Specific sub categories within capex and opex, with corresponding assessment framework and methods (different working groups for each sub category),
- A transparent three-stage assessment approach which allows for the service provider to submit variations,
- Ex post to assess over/under spend with appropriate penalty and incentives, and
- Historical data for benchmarking (to be built up over time), especially for recurring expenditure (already addressed).

¹¹ AER Better Regulation factsheet – expenditure forecast assessment guideline

¹² AER Expenditure forecast assessment guideline - Electricity distribution - August 2022

¹³ AER Expenditure Forecast Assessment Guideline - Explanatory Statement