

PREAMBLE

Background to Draft Decision

Code Requirements

The current access arrangement expires on 30 June 2006. In accordance with the Gas Code, Envestra submitted a revised access arrangement on 30 September 2005.

The Code requires that a draft decision and a final decision be prepared as part of the approval process. Given the need to consult on the revised access arrangement submitted by Envestra and the Authority's Draft Decision, and to allow Envestra to respond to the Authority's Final Decision, it was necessary for the Draft Decision to be released no later than early 2006. To do otherwise would result in the 1 July 2006 deadline for approval of a revised access arrangement being missed or for there to be inadequate consultation with stakeholders.

Authority's Approach and Reservations

The Authority appointed consultants to provide advice on key issues, namely demand, rate of return and the appropriateness of capital and non-capital expenditure.

The Authority received final reports from its consultants from 23 November 2005 through to 7 December 2005.

As a result, the Authority has had limited time in which to prepare this Draft Decision. In addition, the Authority has experienced difficulty in securing from Envestra information at the level of detail that it believes necessary for it to be able to approve some of the claims Envestra has made.

This was a particular issue with respect to some quite significant increases in capital and non-capital costs.

At several points, the Authority has made draft decisions provisional on the information provided to date and has openly invited Envestra to bring forward arguments, detailed project assessments and supporting evidence to substantiate expenditure proposals.

As a result, there are a number of gaps in the analysis and the financial information presented in this Draft Decision.

The Draft Decision is therefore more of a guide to the Authority's thinking and direction rather than a definitive statement of the Authority's most likely position.

The Authority seeks comments from interested parties by 27 February 2006. The Authority is currently planning to release its Final Decision in May 2006 which will be followed by a further brief period of public consultation.

Decision

Asset Base

The Authority has determined an opening asset base, as at 1 July 2006, for Envestra of \$233.8 million. In doing so, the Authority has included virtually all capital expenditure by Envestra during the current regulatory period.

For the next regulatory period, the Authority has (so far) accepted \$66.7 million of capital expenditure for Envestra.

This compares with an opening asset base, as at 1 July 2006, proposed by Envestra of \$236.0 million and forecast capital expenditure of \$102.5 million.

Operating Costs

The Authority has approved \$66.0 million of operating costs for Envestra.

The Authority is concerned by the disparity in operating costs between Allgas and Envestra. Both have fairly similar networks yet Envestra proposed that its operating cost requirement needs to be some 60% higher than that of Allgas.

Rate of Return

The Authority estimated the WACC for Envestra to be 8.75%. That result was very close to the rate proposed by Envestra. While the Authority does not necessarily endorse the methodology used by Envestra to arrive at its proposed WACC, the Authority has decided to accept the rate of return proposed by Envestra. Consequently, Envestra will receive a return of 8.8% on its capital base.

Summary

Overall, the Authority has forecast Envestra will require total revenue of \$172.1 million over the next five years. This amount may change if Envestra is able to bridge the information deficiencies mentioned above.

Based on these revenue requirements, prices for Envestra's smaller volume customers are likely to change by CPI-2.51 per cent each year, while for Envestra's large demand customers prices are likely to vary by CPI-8.10 per cent each year.

These are all average price movements for each customer class and prices to individual customers may vary somewhat about those marks. However, these price paths should be treated with caution and be seen more as a guide than an outcome.