The Hon Patrick Conlon MP
Member for Elder

06MEN/0224

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Dear Dr Walsh

Thank you for your letter of 29 March 2006 regarding the *Proposed Revisions to the Access Arrangement for the South Australian Gas Distribution System: Draft Decision* (Draft Decision).

Consistent with its primary objective under the *Essential Services Commission Act 2002*, in assessing a proposed revised Access Arrangement. The Essential Services Commission of South Australia (ESCOSA) is required, under the National Third Party Access Code for Natural Gas Pipeline Systems (Code), to find a balance between minimising prices to consumers and ensuring Envestra has sufficient resources to meet customer needs, particularly with regard to reliability and security.

ESCOSA's Draft Decision includes a significant increase in the allowance for New Facilities Investment over the period 2006 to 2010 compared with Envestra's actual expenditure in the current Access Arrangement period. The allowance for Non-Capital Costs is largely in line with Envestra's actual expenditure in the current period.

Notwithstanding the significant increase in the allowance for New Facilities Investment, I strongly support the inclusion in the allowance for the SEAGas/MAPS interconnector project, which will assist in promoting gas retail competition in regional areas and ensuring future security of gas supply for South Australia.

Regarding the parameters used by ESCOSA in the calculation of the weighted average cost of capital to be applied to Envestra, the Draft Decision contains a range from 0.8 to 1.0 for the equity beta.

In my submission of 21 November 2005, I noted that Professor Martin Lally of the Victoria University of Wellington, New Zealand, has previously advised the State Government that there was evidence to suggest the use of an equity beta of no more than 0.8 was justified based on his analysis of equity betas of regulated monopolies, including gas distribution businesses. Some studies of recent market data suggest that an equity beta for Australian utilities of substantially lower than 1.0 (possibly as low as 0.5) may be reasonable.

The Draft Decision includes a market risk premium of 6%. Recent work undertaken by the South Australian Centre for Economic Studies for the State Government concluded that a market risk premium in the region of 4.5% to 5% was more appropriate.

Given the relatively flat demand growth assumptions and the significant greenhouse benefits of natural gas, consideration should be given to including strategic New Facilities Investment that would support the sustainability of the network. For example, investment by Envestra in gas refuelling capacity at public transport bus depots could provide valuable energy demand to achieve improved asset utilisation and support the conversion of the public transport bus fleet's fuel source from diesel to compressed natural gas as well as providing opportunities for private vehicles to utilise this fuel type.

Overall, the State Government's view is that ESCOSA has got the balance between cost to consumers and funding of network infrastructure substantially right in its Draft Decision and would expect a similar outcome to be reflected in the Final Decision.

Thank you for this opportunity to make a submission on the Draft Decision.

Yours sincerely

HON PATRICK CONLON MP
MINISTER FOR ENERGY

21 May 2006