

APPENDIX 7

Regulatory audit reports

AGREED-UPON PROCEDURES REPORT ON REVENUE RESET PRO FORMA INFORMATION

REPORT OF FACTUAL FINDINGS

29 May 2008

Transend Networks Pty Ltd
PO Box 606
MOONAH TAS 7009

Australian Energy Regulator
GPO Box 520
Melbourne VIC 3001

Scope

We have performed the procedures agreed with you as detailed in the written instructions of 9 January 2008 and described below with respect to the Revenue Reset Information Pro Formas of Transend Networks Pty Ltd ("Transend") for the half year ended 31 December 2004 and the years ended 30 June 2005, 2006 and 2007.

Our engagement was undertaken in accordance with Australian Auditing Standards applicable to agreed-upon procedures engagements. The responsibility for determining the adequacy or otherwise of the procedures agreed to be performed is that of Transend. The procedures were performed solely to assist you in evaluating your compliance with the National Electricity Rules, and in accordance with Section 2.8 of the Australian Energy Regulator ("AER") Transmission Network Service Provider ("TNSP") Submission Guidelines.

Because the procedures outlined below do not constitute either an audit in accordance with Australian Auditing Standards or a review in accordance with Australian Auditing Standards applicable to review engagements, we do not express any assurance on the Revenue Reset Information Pro Formas of Transend. Had we performed additional procedures or had we performed an audit in accordance with Australian Auditing Standards or a review in accordance with Australian Auditing Standards applicable to review engagements, other matters might have come to our attention that would have been reported to you.

Our procedures and findings are outlined below:

The Basis and Application of the Cost Allocation Methodology

Basis of the Cost Allocation Methodology

(1) We examined the Transend Cost Allocation Methodology Issue 1.0, April 2008 ("the CAM"), set forth in the attached schedules in Appendix A, which applies to:

- Transend's regulatory revenue submission for the regulatory period effective from 1 July 2009 to 30 June 2014; and

- Information provided by Transend to the AER for Transend's submission of its regulatory financial statements for the year ended 30 June 2008,

for compliance with AER Electricity TNSP Cost Allocation Guidelines and therefore Section 6A of the National Electricity Rules ("NER"). We have not examined any Cost Allocation Methodology previously issued by Transend, nor its compliance with AER Electricity TNSP Cost Allocation Guidelines. Our factual findings are outlined below:

- a) We examined the CAM and considered whether its content was described in sufficient detail to enable the AER to replicate reported outcomes. No exceptions were noted.
- b) We examined the CAM to determine whether the substance of the transaction, rather than the legal form of the transaction, has been used to determine the allocation methodology in practice, and this has specifically been referred to in the CAM. We found that the CAM requires per section A2.2 that the substance of the transaction, rather than the legal form of the transaction, is used to determine the allocation.
- c) We examined the CAM to determine whether all costs are to be classified as either a directly attributable cost or a shared cost. We found that the CAM per section A2.3 requires that all costs are to be classified as either a directly attributable cost or a shared cost. In addition, we examined whether the allocation principles for both causal and non causal shared costs are described in the cost allocation principles and policies. We found that, section A2.3.3 of the CAM describes the allocation principles for both causal and non causal shared costs.
- d) We examined the CAM for possible duplication of costs. For example whether there are duplicate costs between direct allocations and shared cost allocations, or across multiple shared cost allocations. We found the following exception:
 - There are costs incurred at the Georgetown substation that are regulated, non-regulated and shared in nature. Management is aware that there are certain costs that have previously been reported as regulated, that are in fact non-regulated. We understand that the split of these costs are immaterial, and the AER has previously been made aware of this issue. We have not validated the materiality (or lack thereof) of this matter represented to us by management.
- e) We compared the CAM to the Transmission Ring-Fencing Guidelines to examine that the contents were consistent. No exceptions were noted.

Application of the Shared Cost Allocation Methodology

- (2) For each year in the scope listed above, we examined whether the Shared Cost Allocation Methodology had been consistently applied to the historical financial information. To complete this step we performed the following:
 - a) Examined that the figures used to allocate the overheads recovered agreed to the audited General Ledger. No exceptions were noted.
 - b) Examined that the allocation of costs as direct or indirect was consistent for each year in scope. No exceptions were noted.
 - c) Examined that the overheads recovered were allocated consistently to the Historical Operating Expenditure categories where the overhead costs were incurred for each year in scope. No exceptions were noted.
- (3) We examined whether the overhead rate was calculated consistently with the CAM. We found that the overhead rate was consistently calculated on the basis of direct labour hours as per section A2.3.3 of the CAM.

Allocation of Operating Expenditure Categories

- (4) For each year in the scope listed above, we examined that the audited General Ledger had been mapped to the appropriate Historical Operating Expenditure categories outlined in Historic Opex Table 1.1. To complete this step we performed the following:
- a) Selected a sample of 10 transactions for each year in the scope listed above. For each transaction we examined the source documentation to see whether the nature of the expense was consistent with the General Ledger and Historical Operating Expenditure categories. No exceptions were noted.
 - b) Re-performed the mapping application to the audited General Ledger Accounts for each year in the scope listed above, and agreed the Operating Expenditure category totals to Historic Opex Table 1.1. No exceptions were noted.
 - c) Examined whether the assumptions in respect of the Labour vs. Non Labour components for Substations, Protection and Control, Transmission Lines and Easements have been consistently applied for each year in the scope listed above. No exceptions were noted. We have not challenged the appropriateness of the Labour vs. Non-Labour assumptions outlined in the table below:

Category	% Labour	% Non-Labour
Substations	65	35
Transmission Lines	70	30
Protection and Control	75	25
Easements	60	40

- i. Examined whether the assumptions in respect of the Field operations and Maintenance components for Substations, Protection and Control, Transmission Lines and Easements have been consistently applied for each year in the scope listed above. No exceptions were noted. We have not challenged the appropriateness of the Field operations and Maintenance assumptions outlined in the table below:

Category	Field operations and maintenance		
	Planned	Condition Assessment	Corrective
Substations	71%	18%	11%
Transmission Lines	71%	24%	5%
Protection and Control	0%	47%	53%
Easements	90%	10%	0%

Allocation of Capital Expenditure Project Categories

- (5) For each year in the scope listed above, we selected 6 Capex Projects and examined whether the allocated Project Category (as detailed in Capex Table 3.1) was in-line with Project Business Cases. No exceptions were noted.

Arithmetic Accuracy

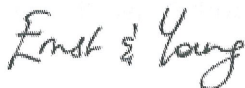
- (1) We examined Opex Tables 1.1 to 1.5 in the Pro Formas, set forth in the attached schedules in Appendix B, for arithmetical accuracy, including all addition and extension formulas and all link formulas. No exceptions were noted.

- (2) We examined Capex Tables 3.1-4 in the Pro Formas, set forth in the attached schedules in Appendix C, for arithmetical accuracy, including all addition and extension formulas and all link formulas. No exceptions were noted.
- (3) We examined the Reconciliation of the Statutory Accounts as reported to the Revised Statutory Accounts, set forth in the attached schedules in Appendix D, for arithmetical accuracy, including all addition and extension formulas and all link formulas. No exceptions were noted.

Reconciliation to Statutory Financial Statements

- (1) We examined whether Transend has maintained its signed, audited financial statements, its disaggregation statements, its regulatory adjustments (between the disaggregation statements and regulatory financial statements) and its signed, audited regulatory financial statements for the years within the above scope. No exceptions were noted.
- (2) We examined management's reconciliation of Historical Opex and Historical Capex in the Pro Forma Schedules to signed, audited Regulatory Financial Statements for each year listed in the scope above. We found the following exceptions:
 - Transend has made retrospective adjustments to the regulated costs previously reported in the 03/04 and 05/06 Regulatory Financial Statements, in its Revenue Cap Application in relation to Superannuation totalling (\$1.639m) and \$1.256, respectively.
 - Transend has made a retrospective adjustment to the regulated costs previously reported in the 05/06 Regulatory Financial Statements, in its Revenue Cap Application in relation to Grid Support Costs totalling (\$1.055m).
 - Transend has made a retrospective adjustment to the regulated costs previously reported in the 06/07 Regulatory Financial Statements in its Revenue Cap Application in relation to Self Insurance Costs totalling (\$0.074m).
 - Transend has made a retrospective adjustment to the regulated costs previously reported in the 03/04 Regulatory Financial Statements in its Revenue Cap Application in relation to an understatement of regulatory costs totalling \$0.244m.
 - Transend has made a retrospective adjustment to the historical capex previously reported in the 03/04, 05/06 and 06/07 Regulatory Financial Statements in its Revenue Cap Application totalling (\$1.157m), (\$0.008m) and (\$1.082m).

Our report is solely for the purpose set forth in the first paragraph of this report and for your information and is not to be used for any other purpose or distributed to any other party. This report relates only to the procedures specified above and does not extend to any financial report of Transend, taken as a whole.



Ernst & Young
Melbourne

29 May 2008