Draft Decision

Ausgrid distribution determination

2015–16 to 2018–19

Attachment 8: Corporate income tax

November 2014

AUSTRALIAN ENERGY REGULATOR

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Note

This attachment forms part of the AER's draft decision on Ausgrid's 2015–19 distribution determination. It should be read with other parts of the draft decision.

The draft decision includes the following documents:

Overview

Attachment 1 – Annual revenue requirement

Attachment 2 – Regulatory asset base

Attachment 3 – Rate of return

Attachment 4 – Value of imputation credits

Attachment 5 – Regulatory depreciation

Attachment 6 – Capital expenditure

Attachment 7 – Operating expenditure

Attachment 8 – Corporate income tax

Attachment 9 – Efficiency benefit sharing scheme

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Attachment 11 – Service target performance incentive scheme

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Attachment 17 – Negotiated services framework and criteria

Attachment 18 – Connection methodology

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Contents

Shortened forms

Shortened form	Extended form
AARR	aggregate annual revenue requirement
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
ASRR	aggregate service revenue requirement
augex	augmentation expenditure
capex	capital expenditure
CCP	Consumer Challenge Panel
CESS	capital expenditure sharing scheme
CPI	consumer price index
CPI-X	consumer price index minus X
DRP	debt risk premium
DMIA	demand management innovation allowance
DMIS	demand management incentive scheme
distributor	distribution network service provider
DUoS	distribution use of system
EBSS	efficiency benefit sharing scheme
ERP	equity risk premium
expenditure assessment guideline	expenditure forecast assessment guideline for electricity distribution
F&A	framework and approach
MRP	market risk premium

Shortened form	Extended form
NEL	national electricity law
NEM	national electricity market
NEO	national electricity objective
NER	national electricity rules
NSP	network service provider
opex	operating expenditure
PPI	partial performance indicators
PTRM	post-tax revenue model
RAB	regulatory asset base
RBA	Reserve Bank of Australia
repex	replacement expenditure
RFM	roll forward model
RIN	regulatory information notice
RPP	revenue pricing principles
SAIDI	system average interruption duration index
SAIFI	system average interruption frequency index
SLCAPM	Sharpe-Lintner capital asset pricing model
STPIS	service target performance incentive scheme
WACC	weighted average cost of capital

8 Corporate income tax

We are required to make a decision on the estimated cost of corporate income tax for Ausgrid's 2014–19 period.[1] Under the post-tax framework, a corporate income tax allowance is calculated as part of the building block assessment using our post-tax revenue model (PTRM). This amount enables Ausgrid to recover the costs associated with the estimated corporate income tax payable during the 2014–19 period.

This attachment presents our assessment of Ausgrid's proposed corporate income tax allowances for the 2014–19 period in respect of its distribution and transmission networks. It also presents our assessment of its proposed opening tax asset bases (TABs), and the standard and remaining tax asset lives used to estimate tax depreciation for the purpose of calculating tax expenses.

8.1 Draft decision

We do not accept Ausgrid's proposed cost of corporate income tax allowances of $636.3 million and $76.0 million ($ nominal) for its distribution and transmission networks respectively. Our draft decision on the estimated cost of corporate income tax is $355.4 million and $36.2 million ($ nominal) for Ausgrid's distribution and transmission networks respectively over the 2014–19 period. This represents a reduction of $280.9 (or 44.1 per cent) for its distribution network and a reduction of $39.8 million (or 52.4 per cent) for its transmission network compared to its proposal.

These reductions reflect our amendments to some of Ausgrid's proposed inputs to forecasting the cost of corporate tax allowance such as the opening TAB (section 8.4.1), and the standard and remaining tax asset lives (section 8.4.2 and section 8.4.3 respectively). It also reflects our draft decision on the value of imputation credits—gamma—(attachment 4). Changes to building block costs affect revenues, which also impact the tax calculation. The changes affecting revenues are discussed in attachment 1.

Table 8-1 and Table 8-2 set out our draft decision on the estimated cost of corporate income tax allowances for Ausgrid's distribution and transmission networks respectively. Based on the approach to modelling the cash flows in the PTRM, we have derived effective tax rates of 24.0 per cent for Ausgrid's distribution network and 19.9 per cent for Ausgrid's transmission network.

Table 8-1 AER's draft decision on Ausgrid's cost of corporate income tax allowance for the 2014–19 period – distribution ($ million, nominal)

	2014–15	2015–16	2016–17	2017–18	2018–19	Total
Tax payable	103.2	113.8	132.6	122.1	120.6	592.4
Less: value of imputation credits	41.3	45.5	53.0	48.8	48.3	237.0
Corporate income tax allowance	**61.9**	**68.3**	**79.5**	**73.3**	**72.4**	**355.4**

Source: AER analysis.

[1] NER, cl. 6.4.3(a)(4).

Table 8-2 AER's draft decision on Ausgrid's cost of corporate income tax allowance for the 2014–19 period – transmission ($ million, nominal)

	2014–15	2015–16	2016–17	2017–18	2018–19	Total
Tax payable	10.7	11.5	13.0	12.7	12.4	60.3
Less: value of imputation credits	4.3	4.6	5.2	5.1	5.0	24.1
Corporate income tax allowance	6.4	6.9	7.8	7.6	7.4	**36.2**

Source: AER analysis.

8.2 Ausgrid's proposal

Ausgrid proposed forecast cost of corporate income tax allowances of $636.3 million and $76.0 million ($ nominal) for its distribution and transmission networks respectively, calculated using the AER's PTRM and the following inputs:[2]

- opening TABs as at 1 July 2014 of $8401.2 million and $1631.0 million ($ nominal) for its distribution and transmission networks respectively
- an expected statutory income tax rate of 30 per cent per year
- a value for gamma of 0.25.
- remaining tax asset lives of assets in existence as at 30 June 2014, calculated based on the standard tax asset life for an asset class multiplied by the ratio of the regulatory asset base (RAB) remaining asset life to the RAB standard asset life[3]
- the same standard tax asset lives for depreciating new assets for the 2014–19 regulatory control period as approved at the 2009–14 regulatory control period.

2 Ausgrid, *Regulatory proposal*, May 2014, Attachment 4.01 and Attachment 4.02.
3 Ausgrid, *Regulatory proposal*, May 2014, Attachment 4.08.

Table 8-3 and Table 8-4 set out Ausgrid's proposed cost of corporate income tax allowances for its distribution and transmission networks respectively over the 2014–19 period.

Table 8-3 Ausgrid's proposed cost of corporate income tax allowance for the 2014–19 period – distribution ($ million, nominal)

	2014–15	2015–16	2016–17	2017–18	2018–19	Total
Tax payable	143.1	157.7	183.5	179.8	184.4	848.4
Less: value of imputation credits	35.8	39.4	45.9	45.0	46.1	212.1
Corporate income tax allowance	**107.3**	**118.2**	**137.6**	**134.9**	**138.3**	**636.3**

Source: Ausgrid, *Regulatory proposal*, May 2014, Attachment 4.01.

Table 8-4 Ausgrid's proposed cost of corporate income tax allowance for the 2014–19 period – transmission ($ million, nominal)

	2014–15	2015–16	2016–17	2017–18	2018–19	Total
Tax payable	17.8	19.2	21.6	21.1	21.6	101.3
Less: value of imputation credits	4.5	4.8	5.4	5.3	5.4	25.3
Corporate income tax allowance	**13.4**	**14.4**	**16.2**	**15.8**	**16.2**	**76.0**

Source: Ausgrid, *Regulatory proposal*, May 2014, Attachment 4.02.

8.3 AER's assessment approach

Under clause 6.5.3 of the National Electricity Rules (NER), we must make an estimate of taxable income for each regulatory year. Our estimate must be for the taxable income a benchmark efficient entity would earn for providing standard control services if it operated Ausgrid's business. The estimate is required to be determined in accordance with the PTRM. Our approach for calculating a service provider's cost of corporate income tax allowance is set out in our PTRM and involves the following steps:

1. We estimate the annual taxable income that would be earned by a benchmark efficient entity operating the service provider's business. A service provider's taxable income is calculated by subtracting from the approved forecast revenues the benchmark estimates of tax expenses. Using the PTRM, we model the service provider's benchmark tax expenses, including interest tax expense and tax depreciation, over the regulatory control period. The interest tax expense is estimated using the benchmark 60 per cent gearing used for the rate of return calculation. Tax depreciation is calculated using a separate value for the TAB, and standard and remaining tax asset lives for taxation purposes. All tax expenses (including other expenses such as opex) are offset against the service provider's forecast revenue to estimate the taxable income.

2. The statutory income tax rate is then applied to the estimated annual taxable income to arrive at a notional amount of tax payable.

3. We apply a discount to that notional amount of tax payable to account for the utilisation of imputation credits (gamma) by investors.

4. The tax payable net of assumed utilised imputation credits represents the corporate income tax allowance and is included as a separate building block in determining the service provider's annual revenue requirement.

The cost of corporate income tax allowance is an output of our PTRM. We therefore assess the service provider's proposed cost of corporate tax allowance by analysing the proposed inputs to the PTRM for calculating that allowance. These inputs include:

- **The opening TAB as at the commencement of the 2014–19 period:** We consider that the roll forward of the opening TAB should be based on the approved opening TAB as at commencement of the 2009–14 regulatory control period and the service provider's actual capex incurred during the 2009–14 regulatory control period.[4]
- **The remaining tax asset life for each asset class at the commencement of the 2014-19 period:** Our preferred method to determine the remaining tax asset lives is the weighted average method. We consider the weighted average method provides a better reflection of the mix of assets within an asset class. We will assess the outcomes of other approaches against the outcomes of this preferred method.
- **The standard tax asset life for each asset class:** We assess the service provider's proposed standard tax asset lives, where necessary, against those prescribed by the Commissioner for taxation in tax ruling 2014/4 and the approved standard tax asset lives in the service provider's distribution determination for the 2009–14 regulatory control period.
- **The income tax rate:** The statutory income tax rate is 30 per cent per year.
- **The value of gamma:** The gamma input for Ausgrid is 0.40. Refer to attachment 4 for detailed discussion on this matter.

8.3.1 Interrelationships

The cost of corporate income tax building block feeds directly into the annual revenue requirement (ARR). This allowance is determined by four factors:

- pre-tax revenues
- tax expenses (including tax depreciation)
- the corporate tax rate
- gamma—the expected proportion of company tax that is returned to investors through the utilisation of imputation credits—which is offset against the corporate income tax allowance. This is discussed further at attachment 4.

Of these four factors, the corporate tax rate is set externally by the Government. The higher the tax rate the higher the required tax allowance.

The pre-tax revenues depend on all the building block components. Any factor that affects revenue will therefore affect pre-tax revenues. Higher pre-tax revenues can increase the tax allowance.[5]

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[4] The tax depreciation is therefore recalculated based on actual capex. The same tax depreciation approach of using actual capex applies to the roll forward of the TAB at the next reset.

[5] In fact, there is an iterative relationship between tax and revenues. That is, revenues lead to tax, being applied, which increases revenues and leads to slightly more tax and so on. The PTRM is therefore set up to run an iterative process until the revenue and tax allowances become stable.

Depending on the source of the revenue increase, the tax increase may be equal to or less than proportional to the company tax rate.[6]

The tax expenses depend on various building block components and their size. Some components give rise to tax expenses, such as opex, interest payments and tax depreciation of assets. However, others do not, such as increases in return on equity. Higher tax expenses offset revenues as deductions in the tax calculation and therefore reduce the cost of corporate income tax allowance (all things being equal). Tax expenses include:

- Interest on debt – Interest is a tax offset. The size of which depends on the ratio of debt to equity and therefore the proportion of the RAB funded through debt. It also depends on the allowed return on debt and the size of the RAB.
- General expenses – In the main these expenses will match the opex allowance.
- Tax depreciation – A separate TAB is maintained for the businesses reflecting tax rules. This TAB is affected by many of the same factors as the RAB, such as capex, although unlike the RAB value it is maintained at its historical cost with no indexation. The TAB is also affected by the depreciation rate and asset lives assigned for tax depreciation purposes.

A ten per cent increase in the corporate income tax allowance causes revenues to increase by about 0.6 per cent. The proposed gamma of 0.25, compared to the value in our draft decision of 0.4, would increase the corporate income tax allowance by 24 per cent and total revenues by about 1.4 per cent.

8.4 Reasons for draft decision

We do not accept Ausgrid's proposed cost of corporate income tax allowances. We have instead determined a cost of corporate income tax allowance of $355.4 million and $36.2 million ($nominal) for its distribution and transmission networks respectively. These represent reductions of $280.9 million (or 44.1 per cent) for Ausgrid's distribution network and $39.8 million (or 52.4 per cent) for Ausgrid's transmission network.

This is because we adjusted the following proposed inputs to the distribution and transmission PTRMs for tax purposes:

- the opening TAB values as at 1 July 2014 (section 8.4.1)
- the standard and remaining tax asset lives (sections 8.4.2 and 8.4.34.3)
- the value of gamma (attachment 4)
- other building block components including forecast opex (attachment 7) and forecast capex (attachment 6) that effect revenues, and therefore also impact the forecast corporate income tax allowance.[7]

8.4.1 Opening tax asset base

We do not accept Ausgrid's proposed opening TABs as at 1 July 2009 of $8401.2 million for its distribution network and $1631.0 million ($nominal) for its transmission network. Instead we determine

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[6] For example, although increased opex adds to revenue requirement, these expenses are also offset against the revenues as deductions in determining tax, so there is no net impact in this case. A higher return on equity, in contrast, gives rise to no offsetting tax expenses and therefore increases the tax allowance in proportion to the company tax rate.

[7] NER, cl 6.5.3.

the opening TABs as at 1 July 2014 of $8562.4 million and $1502.1 million for Ausgrid's distribution and transmission networks respectively. These differences are caused by:

- adjustments for the difference in actual and estimated capex for 2008–09. This estimate was included in the approved opening TAB as at 1 July in the 2009 determination.
- adjustments to the tax depreciation for the 2009–14 regulatory control period due to the difference between actual and estimated capex for 2008–09
- correction of Ausgrid's actual net capex inputs for errors associated with the value of asset disposals and capital contributions, including updates for the estimate of capex for 2013–14
- correction of a formula error in the RFM used to calculate the tax depreciation for IT system assets.

To determine the opening TABs as at 1 July 2014, we have rolled forward the TABs over the 2009–14 regulatory control period to determine closing TABs at 30 June 2014. For the distribution TAB, from 1 July 2014, metering will be classified as an alternative control service and therefore metering assets have been removed from the standard control services TAB as discussed in attachment 16. The reasons for our decision on Ausgrid's opening TABs for its distribution and transmission networks are set out below.

Opening TAB as at 1 July 2009

We do not accept Ausgrid's proposed opening TABs of $4552.9 million and $645.5 million ($ nominal) as at 1 July 2009 for its distribution and transmission networks respectively. Ausgrid proposed to update the opening TABs as at 1 July 2009 for the actual capex for 2008–09.[8,9] We reviewed Ausgrid's proposed opening TABs as at 1 July 2009 with respect to the difference in actual and estimated capex for 2008–09. We identified the following:

- Ausgrid's proposed distribution opening TAB was $190.0 million higher than the approved value (based on estimated capex for 2008–09 at the time) as at 1 July 2009.
- Ausgrid's proposed transmission opening TAB was $11.0 million higher than the approved value (based on estimated capex for 2008–09 at the time) as at 1 July 2009.

However, these differences do not appear to match the difference between actual and estimated capex for 2008–09. We note:

- For Ausgrid's distribution network the actual capex for 2008–09 was $296.5 million ($ nominal) higher than estimated.
- For Ausgrid's transmission network the actual capex for 2008–09 was $63.6 million ($ nominal) lower than estimated.

Table 8-5 compares the difference between Ausgrid's proposed distribution opening TAB and the approved opening TAB as at 1 July 2009 with the difference between actual and estimated capex for 2008–09.

8 For tax purposes actual capex is gross capex including capital contribution less asset disposals.
9 Ausgrid, *Regulatory proposal*, June 2014, Attachment 4.08.

Table 8-5 Ausgrid's opening TAB as at 1 July 2009: approved vs proposed and difference between 2008–09 actual and estimated capex ($million, nominal) – distribution

Ausgrid's distribution network – tax asset base	
Ausgrid proposed opening TAB – 1 July 2009	4 552.8
Ausgrid approved opening TAB – 1 July 2009	4 362.9
Difference	**190.0**
Actual capex for 2008–09[a]	1 180.6
Estimated capex for 2008–09[a]	884.2
Difference	**296.5**

Source: AER analysis.
(a) Capex for the TAB includes capital contributions and is calculated as gross capex less disposals.

Table 8-6 compares the difference between Ausgrid's proposed transmission opening TAB and the approved opening TAB as at 1 July 2009 with the difference between actual and estimated capex for 2008–09.

Table 8-6 Ausgrid's opening TAB as at 1 July 2009: approved vs proposed and difference between 2008–09 actual and forecast capex ($million, nominal) – transmission

Ausgrid's transmission network – tax asset base	
Ausgrid proposed opening TAB – 1 July 2009	645.9
Ausgrid approved opening TAB – 1 July 2009	634.9
Difference	**11.0**
Actual capex 2008–09[a],	96.8
Estimated capex 2008–09[a]	160.4
Difference	**–63.6**

Source: AER analysis.
(a) Actual capex for TAB includes capital contributions and is calculated as gross capex less disposals.

Based on the above, we consider the proposed opening TABs as at 1 July 2009 should be adjusted to properly reflect the difference between the actual and estimated capex for 2008–09. For Ausgrid's distribution opening TAB as at 1 July 2009 we added $296.5 million ($ nominal) to reflect the capex overspend. For Ausgrid's transmission opening TAB as at 1 July 2009 we removed the capex underspend of $63.6 million ($ nominal). We therefore determine opening TABs of $4659.4 million and $570.9 million ($ nominal) as at 1 July 2009 for Ausgrid's distribution and transmission network respectively.

Depreciation adjustment 2009–10 to 2013–14

We do not accept Ausgrid's proposed actual tax depreciation over the 2009–14 regulatory control period for its distribution and transmission networks. This is because of our adjustments to Ausgrid's proposed opening TABs as at 1 July 2009.

Our 2009 determination for Ausgrid did not contain remaining tax asset lives for depreciating its opening TABs as at 1 July 2009. Instead, we approved the use of specific forecast tax depreciation

amounts for the 2009–14 regulatory control period based on the opening TAB as at 1 July 2009 approved in the 2009 determination.[10]

For this draft decision, we updated the forecast tax depreciation on the approved opening TABs as at 1 July 2009 to account for actual capex for 2008–09. To adjust the forecast tax depreciation on the opening TAB as at 1 July 2009 over the 2009–14 period to reflect actual capex we:

- calculated the difference between the actual and estimated capex (net of asset disposals) for 2008–09 for each asset class
- calculated one year of tax depreciation on the difference between actual and estimated capex for 2008–09 by dividing with the standard tax asset life
- added one year of tax depreciation associated with the difference between actual and estimated capex for 2008–09 to the forecast depreciation on the opening TAB for each year of the 2009–14 regulatory control period.

We consider our approach provides for the appropriate amount of tax depreciation associated with the opening TABs as at 1 July 2009 after adjusting for actual capex for 2008–09. This is consistent with the operation of our RFM[11] and provides an appropriate estimate of the actual tax depreciation over the 2009–14 regulatory control period.

Actual capex 2009–10 to 2012–13

For the reasons discussed in attachment 2, we have updated Ausgrid's proposed roll forward of its TABs in the RFM to correct for errors that affect the value of actual net capex from 2009–10 to 2012–13. This involved updates for the value of actual capex (gross), the value of asset disposals and capital contributions. The reasons for these amendments to Ausgrid's actual net capex inputs for its distribution and transmission networks are detailed further where we discuss the RAB.

Estimated capex for 2013–14

For the reasons discussed in attachment 2, Ausgrid provided revised estimates of inputs for 2013–14 reflecting actual capex, disposals and capital contributions.[12] We have adopted these values in the RFM for the draft decision and will treat them as revised estimates. For Ausgrid's distribution network the revised capex net of disposals for 2013–14 changes to $634.2 million from $680.5 million ($ nominal). Ausgrid's revised actual capex net of disposals for its transmission network for 2013–14 changes to $82.1 million from $143.6 million ($ nominal). We will check these values with the audited annual reporting RIN to be received in late 2014 as part of the final decision.

IT systems tax depreciation 2009–10 to 2013–14

We do not accept Ausgrid's proposed closing tax asset value for the 'IT systems' asset class as at 30 June 2014. Ausgrid proposed closing tax asset values for the 'IT systems' asset class of $88.0 million and $12.6 million ($ nominal) for its distribution and transmission networks respectively. We reviewed Ausgrid's distribution and transmission RFMs and identified a formula error in the calculation of tax depreciation on capex for this asset class over the 2009–14 regulatory control period.[13] After correcting for the formula error and adjusting for the inputs discussed above, we have determined an

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10 AER, *Draft Decision - NSW draft distribution determination 2009–10 to 2013–14*, 21 November 2008, p. 207.
11 AER, *Electricity distribution network service providers Roll forward model handbook*, June 2008 , p. 7.
12 Ausgrid, *Email response to AER AUSGRID 024*, 29 August 2014.
13 Ausgrid, *Email response to AER AUSGRID 014*, 21 July 2014.

closing tax asset values for the 'IT systems' asset class of $102.6 million for distribution and $14.5 million ($ nominal) for transmission as at 30 June 2014.[14]

Removal of metering assets as at 1 July 2014

We do not accept Ausgrid's proposed adjustment of $232.6 million ($ nominal) to remove metering assets from the closing distribution TAB as at 30 June 2014 due to the change in classification of metering services to alternative control services. Our adjustments to Ausgrid's distribution TAB discussed above altered the closing values of the asset classes and therefore affected the amount of metering assets to be removed.

We reviewed and were satisfied with the appropriateness of Ausgrid's revised allocation of metering assets for the distribution RAB to be moved to metering alternative control services as discussed in attachment 16. We have adopted this approach for making the adjustment to the closing TAB as at 30 June 2014 for the purposes of this draft decision. In applying Ausgrid's revised allocation we determine an adjustment of $242.8 million ($ nominal) to reflect the proportion of the TAB associated with metering assets moving to alternative control services.

Opening TAB as at 1 July 2014

We are satisfied the above adjustments result in opening TABs as at 1 July 2014 for Ausgrid's distribution and transmission networks that provide estimates of tax depreciation consistent with the tax expenses used to estimate the annual taxable income of a benchmark efficient entity over the 2014–19 period.[15] We therefore determine opening TABs of $8562 million and $1502 million ($ nominal) as at 1 July 2014 for Ausgrid's distribution and transmission networks respectively.

For the reasons discussed in attachment 5, we have also removed the 'Emergency spares (major plant, excludes inventory)' and 'Transmission & zone emergency spares' asset classes from the PTRMs for Ausgrid's distribution and transmission networks respectively. For Ausgrid's distribution PTRM we reallocated the remaining value in 'Emergency spares (major plant, excluding inventory)' to the 'Substations asset class. For Ausgrid's transmission PTRM we reallocated the remaining value in 'Transmission & zone emergency spares' to the 'Transmission zone substation equipment 132/66kV' and 'Zone substation equipment 132/66kV' asset classes. The reallocation has no effect on the total opening TAB values as at 1 July 2014 for Ausgrid's distribution and transmission networks, and removes these unused legacy assets classes from the PTRMs.

[14] The closing tax asset value in the 'IT systems' asset class as at 30 June 2014 for distribution does not account for the adjustment for assets to be moved to metering alternative control services.

[15] NER, cl. 6.5.3.

Table 8-7 and Table 8-8 sets out our draft decision on the roll forward of Ausgrid's TABs over the 2009–14 regulatory control period for its distribution and transmission network respectively.

Table 8-7 AER's draft decision on Ausgrid's TAB roll forward – distribution ($ million, nominal)

	2009–10	2010–11	2011–12	2012–13	2013–14[b]
Opening TAB	4 659.4	5 485.1	6 574.8	7 709.3	8 488.6
Capital expenditure[a]	1 124.5	1 313.3	1 398.1	1 078.8	634.2
Less: tax depreciation	298.8	224.6	262.6	299.5	316.7
Closing TAB	5 485.1	6 574.8	7 709.3	8 488.6	8 805.2
Meters moved to alternative control services					–242.8
Opening TAB as at 1 July 2014					**8 562.4**

Source: AER analysis.
(a) Net of disposals.
(b) Based on revised estimated capex.

Table 8-8 AER's draft decision on Ausgrid's TAB roll forward – transmission ($ million, nominal)

	2009–10	2010–11	2011–12	2012–13	2013–14[b]
Opening TAB	570.9	761.9	1 001.8	1 296.5	1 463.8
Capital expenditure[a]	223.9	264.6	325.9	206.3	82.1
Less: tax depreciation	32.9	24.7	31.2	39.0	43.8
Closing TAB	761.9	1 001.8	1 296.5	1 463.8	1 502.1

Source: AER analysis.
(a) Net of disposals.
(b) Based on estimated capex.

8.4.2 Standard tax asset lives

We accept the majority of Ausgrid's proposed standard tax asset lives for its distribution and transmission networks because they are:

- broadly consistent with the values prescribed by the Commissioner for taxation in tax ruling 2014/4[16]
- the same as those approved standard tax asset lives for the 2009–14 regulatory control period.

We are satisfied that the proposed standard tax asset lives remain appropriate for applying over the 2014–19 period.

However, we have changed the standard tax asset life for the 'Equity raising costs' asset class to 5 years from Ausgrid's proposed 47.3 years (distribution) and 45.7 years (transmission) for tax depreciation purposes. This is because the Australian Taxation Office (ATO) requires equity raising

[16] ATO, *Taxation Ruling Income tax: effective life of depreciating assets* (applicable from 1 July 2014), August 2014, http://law.ato.gov.au/atolaw/view.htm?docid=%22TXR%2FTR20144%2FNAT%2FATO%2F00001%22, accessed on 25 September 2014.

costs to be amortised over a five-year period on a straight-line basis.[17] In recent determinations, we adopted a standard tax asset life of 5 years for amortising equity raising costs for tax depreciation purposes. Therefore, we will apply the standard tax asset life of 5 years for tax depreciation purposes.[18] We consider this standard tax asset life provides a better estimate of the tax depreciation amount for a benchmark efficient service provider as required by the NER.[19]

Table 8-9 and Table 8-10 present our draft decision on the standard tax asset lives for Ausgrid's distribution and transmission networks respectively.

8.4.3 Remaining tax asset lives

We accept Ausgrid's proposed remaining tax asset lives for its distribution and transmission networks as at 1 July 2014. Our 2009 determination for Ausgrid did not contain remaining tax asset lives for depreciating its opening TAB as at 1 July 2009. Instead, we approved the use of specific forecast tax depreciation amounts for the 2009–14 regulatory control period.[20] Ausgrid proposed remaining tax asset lives as at 1 July 2014 calculated based on the standard tax asset life for an asset class multiplied by the ratio of the RAB remaining asset life to the RAB standard asset life.[21]

We reviewed Ausgrid's proposed approach against alternative methods to establish the remaining tax asset lives as at 1 July 2014. We found Ausgrid's proposed approach provides reasonable estimates of remaining tax asset lives for the majority of Ausgrid's asset classes. We consider that Ausgrid's proposed approach aligns the cash flows associated with the estimate of tax depreciation with the expected life of the network. This is because for the majority of asset classes the standard asset lives for Ausgrid's RAB are comparable to the standard tax asset lives. We are therefore satisfied that the proposed approach results in an estimate of tax depreciation consistent with the tax expenses used to estimate the annual taxable income of a benchmark efficient entity over the 2014–19 period.[22]

In accepting Ausgrid's approach to establish the remaining tax asset lives as at 1 July 2014, we have updated the proposed remaining tax asset lives consistent with the adjustments to the RAB remaining asset lives as at 1 July 2014, discussed in attachment 5.[23] This is because Ausgrid's approach to calculate the remaining tax asset life uses the ratio of the RAB remaining asset life to the RAB standard asset life.[24]

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17 ATO, *Guide to depreciating assets 2001-02: Business related costs—section 40-880 deductions*, ATO reference; NO NAT7170, p. 25.

18 AER, Draft decision: *Powerlink transmission determination 2012–13 to 2016–17*, 2011, p. 265–266; AER, *Draft decision: ElectraNet transmission determination 2013–14 to 2017–18*, 2013, p. 193–194.

19 NER, cl. 6.5.3.

20 AER, *Draft Decision - NSW draft distribution determination 2009–10 to 2013–14*, 21 November 2008, p. 207.

21 Ausgrid, *Regulatory proposal*, May 2014, Attachment 4.08

22 NER, cl. 6.5.3.

23 Having established the remaining tax asset lives as at 1 July 2014 for this determination process, we consider that when rolling forward these remaining tax asset lives to 1 July 2019 at the next reset our preferred weighted average method should be used.

24 We may update the tax remaining asset lives as at 1 July 2014, if there are updates to the RAB remaining asset lives arising from revisions to the 2013–14 capex at the final decision.

Table 8-9 and Table 8-10 respectively present our draft decision on the remaining tax asset lives for Ausgrid's distribution and transmission networks as at 1 July 2014.

Table 8-9 AER's draft decision on Ausgrid's standard and remaining tax asset lives as at 1 July 2014 (years) – distribution

Asset class	Standard tax asset life	Remaining tax asset life as at 1 July 2014
Sub-transmission lines and cables	47.5	33.7
Cable tunnel (dx)	40.0	38.5
Distribution lines and cables	48.7	39.3
Substations	40.0	29.7
Transformers	42.0	27.9
Low voltage lines and cables	45.8	35.2
Customer metering and load control	25.0	14.5
Communications (digital) - dx	10.0	5.6
Total communications	7.4	2.2
System IT (dx)	7.0	4.9
Ancillary substations equipment (dx)	15.0	12.4
Land and easements	n/a	n/a
Furniture, fittings, plant and equipment	10.60	7.6
Land (non-system)	n/a	n/a
Other non-system assets	10.5	2.7
IT systems	4.0	2.6
Motor vehicles	20.0	12.3
Buildings	40.0	33.4
Equity raising costs	5.0	43.4

Source: AER analysis.
n/a: not applicable.

Table 8-10 AER's draft decision on Ausgrid's standard and remaining tax asset lives as at 1 July 2014 (years) – transmission

Asset class	Standard tax asset life	Remaining tax asset life as at 1 July 2014
Transmission & Zone land & easements	n/a	n/a
Transmission buildings	40.0	30.6
Zone buildings 132/66kV	40.0	33.3
Transmission transformers 132/66kV	40.0	29.5

Zone transformers 132/66kV	45.0	30.6
Transmission substation equip 132/66kV	40.0	30.3
Zone substation equip 132/66kV	40.0	33.5
Ancillary substation equipment (tx)	15.0	13.9
132kV tower lines	47.6	33.7
132kV concrete & steel pole lines	47.6	40.5
132kV wood pole lines	47.6	31.9
132kV feeders underground	47.0	38.2
Cable tunnel (tx)	47.6	40.9
Network control & com systems	37.2	17.5
Communications (digital) - tx	10.0	7.9
System IT (tx)	7.0	4.8
IT systems	4.0	2.6
Furniture, fittings, plant and equipment	10.6	7.6
Motor vehicles	20.0	12.3
Buildings	40.0	33.4
Land (non-system)	n/a	n/a
Other non-system assets	10.5	2.7
Equity raising costs	5.0	41.7

Source: AER analysis.
n/a: not applicable.