

FINAL DECISION

TransGrid transmission determination

2015−16 to 2017−18

Attachment 8 – Corporate income tax

April 2015

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1. Note
2. This attachment forms part of the AER's final decision on TransGrid’s revenue proposal 2015–18. It should be read with other parts of the final decision.
3. The final decision includes the following documents:
4. Overview
5. Attachment 1 – maximum allowed revenue
6. Attachment 2 – regulatory asset base
7. Attachment 3 – rate of return
8. Attachment 4 – value of imputation credits
9. Attachment 5 – regulatory depreciation
10. Attachment 6 – capital expenditure
11. Attachment 7 – operating expenditure
12. Attachment 8 – corporate income tax
13. Attachment 9 – efficiency benefit sharing scheme
14. Attachment 10 – capital expenditure sharing scheme
15. Attachment 11 – service target performance incentive scheme
16. Attachment 12 – pricing methodology
17. Attachment 13 – pass through events

Attachment 14 – negotiated services

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1. Shortened forms

| 1. Shortened form | 1. Extended form |
| --- | --- |
| 1. AARR | 1. aggregate annual revenue requirement |
| 1. AEMC | 1. Australian Energy Market Commission |
| 1. AEMO | 1. Australian Energy Market Operator |
| 1. AER | 1. Australian Energy Regulator |
| 1. ASRR | 1. annual service revenue requirement |
| 1. augex | 1. augmentation expenditure |
| 1. capex | 1. capital expenditure |
| 1. CCP | 1. Consumer Challenge Panel |
| 1. CESS | 1. capital expenditure sharing scheme |
| 1. CPI | 1. consumer price index |
| 1. DRP | 1. debt risk premium |
| 1. EBSS | 1. efficiency benefit sharing scheme |
| 1. ERP | 1. equity risk premium |
| 1. MAR | 1. maximum allowed revenue |
| 1. MRP | 1. market risk premium |
| 1. NEL | 1. national electricity law |
| 1. NEM | 1. national electricity market |
| 1. NEO | 1. national electricity objective |
| 1. NER | 1. national electricity rules |
| 1. NSP | 1. network service provider |
| 1. NTSC | 1. negotiated transmission service criteria |
| 1. opex | 1. operating expenditure |
| 1. PPI | 1. partial performance indicators |
| 1. PTRM | 1. post-tax revenue model |
| 1. RAB | 1. regulatory asset base |
| 1. RBA | 1. Reserve Bank of Australia |
| 1. repex | 1. replacement expenditure |
| 1. RFM | 1. roll forward model |
| 1. RIN | 1. regulatory information notice |
| 1. RPP | 1. revenue and pricing principles |
| 1. SLCAPM | 1. Sharpe-Lintner capital asset pricing model |
| 1. STPIS | 1. service target performance incentive scheme |
| 1. TNSP | 1. transmission network service provider |
| 1. TUoS | 1. transmission use of system |
| 1. WACC | 1. weighted average cost of capital |

# Corporate income tax

1. The AER is required to make a decision on the estimated cost of corporate income tax for TransGrid's 2014–18 period.[[1]](#footnote-1) Under the post-tax framework, a corporate income tax allowance is calculated as part of the building block assessment using the post-tax revenue model (PTRM).
2. This attachment sets out our final decision on TransGrid's revised proposed corporate income tax allowance. It also presents our final decision on the revised proposed opening tax asset base (TAB), and the standard and remaining tax asset lives used to estimate tax depreciation for the purpose of calculating tax expenses.

## Final decision

We accept TransGrid's proposed approach to estimating its cost of corporate income tax. We determine TransGrid's corporate income tax allowance to be $101.5 million ($ nominal) for the 2014–18 period. This represents a reduction of $105.8 million (or 51.0 per cent) from TransGrid's revised proposal.

Our final decision differs from TransGrid's revised proposal due to our determination on TransGrid's proposed value of imputation credits (gamma) as discussed in attachment 4. Our determinations on other building block components including forecast capex (attachment 6) and forecast opex (attachment 7) affect revenues, which also impact the tax calculation.

1. Table 8‑1 sets out our final decision on the estimated cost of corporate income tax allowance for TransGrid.

Table 8‑1 AER's final decision on TransGrid's cost of corporate income tax allowance for the 2014–18 period ($ million, nominal)

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 2014–15 | 2015–16 | 2016–17 | 2017–18 | Total |
| Tax payable | 28.6 | 31.3 | 54.4 | 54.9 | 169.2 |
| Less: value of imputation credits | 11.4 | 12.5 | 21.8 | 22.0 | 67.7 |
| **Net corporate income tax allowance** | **17.1** | **18.8** | **32.6** | **33.0** | **101.5** |

Source: AER analysis.

## TransGrid’s revised proposal

1. TransGrid's methodology for determining its corporate income tax is unchanged from its initial proposal. We accepted the approach in our draft decision. TransGrid has revised its corporate income tax allowance using the AER's PTRM and included the following inputs:[[2]](#footnote-2)

* A revised opening TAB at 1 July 2014, reflecting updates for 2013–14 actual capex.
* Revised forecast capex.
* Revised forecast opex.

TransGrid also used the standard tax asset lives consistent with those approved in the draft decision and remaining tax asset lives reflecting updates for 2013–14 actual capex and a value for gamma of 0.25 consistent with its initial proposal.

Due to the revised inputs, TransGrid's corporate income tax allowance is $23.2 million (or 10.1 per cent) lower in its revised proposal than in its initial proposal.

1. Table 8‑2 sets out TransGrid's revised proposed corporate income tax allowance for the 2014–18 period.

Table 8‑2 TransGrid's revised proposed corporate income tax allowance for the 2014–18 period ($ million, nominal)

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 2014–15 | 2015–16 | 2016–17 | 2017–18 | Total |
| Tax payable | 52.4 | 56.7 | 82.7 | 84.5 | 276.3 |
| Less: value of imputation credits | 13.1 | 14.2 | 20.7 | 21.1 | 69.1 |
| **Net corporate income tax allowance** | **39.3** | **42.5** | **62.0** | **63.4** | **207.2** |

Source: TransGrid, Revised revenue proposal, January 2015, p. 130.

## AER’s assessment approach

We did not change our assessment approach for the corporate income tax allowance from our draft decision. Section 8.3 of our draft decision details that approach.

## Reasons for final decision

1. We do not accept TransGrid's revised proposed estimated cost of corporate income tax. We instead determine an estimated cost of corporate income tax of $101.5 million ($ nominal) for TransGrid, which represents a reduction of $105.8 million (or 51.0 per cent) from its revised proposal.
2. This reduction is due to the adjustment of proposed inputs to the PTRM which affect the calculation of the taxable income, and therefore the estimated corporate income tax allowance:[[3]](#footnote-3)

* The opening TAB value at the commencement of the 2014–18 period (section Opening tax asset base at 1 July 20148.4.1).
* The remaining tax asset lives (section 8.4.2).
* The value for gamma (attachment 4).
* Our determinations on other building block components, including forecast opex (attachment 7) and forecast capex (attachment 6).

1. We maintain our draft decision acceptance of the standard tax asset lives (section 8.4.2) inputs to the PTRM for tax purposes.[[4]](#footnote-4)

### Opening tax asset base at 1 July 2014

1. We determine TransGrid's opening TAB value as at 1 July 2014 to be $3750.3 million ($ nominal).

In the draft decision, we accepted TransGrid's proposed method for determining the opening TAB as at 1 July 2014, subject to updating for actual capex for 2013–14.

In its revised proposal, TransGrid updated its estimated capex for 2013–14 with actual capex in the roll forward model (RFM). As discussed in attachment 2, we identified a small discrepancy when reconciling these capex inputs with TransGrid's regulatory accounts. In response to our questions, TransGrid acknowledged that there was an indexation error applied in its revised proposal and resubmitted the corrected 2013–14 actual capex value.[[5]](#footnote-5) The correction results in a reduction of $0.5 million to the revised proposed opening TAB value as at 1 July 2014. While this adjustment is small, we have decided to require the change because it was a clear clerical error.

1. Table 8‑3 sets out our final decision on the roll forward of TransGrid's TAB values.

Table 8‑ AER's final decision on TransGrid's TAB roll forward for the 2009–14 regulatory control period ($ million, nominal)

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 2009–10 | 2010–11 | 2011–12 | 2012–13 | 2013–14 |
| Opening TAB | 2718.0 | 2800.8 | 3001.4 | 3189.2 | 3382.8 |
| Capital expenditurea | 221.0 | 345.1 | 345.5 | 362.6 | 553.5 |
| Tax depreciation | –138.3 | –144.4 | –157.7 | –169.0 | –185.9 |
| Closing TAB | 2800.8 | 3001.4 | 3189.2 | 3382.8 | 3750.3 |

Source: AER analysis.

(a) As commissioned, net of disposals.

### Standard and remaining tax asset lives

Consistent with our draft decision, we accept TransGrid's proposed standard tax asset lives, which include the following changes to the standard tax asset lives for:

* 'Underground cables 2014–18' asset class (to 45 years from 50 years).
* 'Secondary systems 2014–18' asset class (to 15 years from 35 years).
* 'Communications 2014–18' asset class (to 10 years from 35 years).
* The new asset class 'Transmission line life extension' of 25 years.

1. In the draft decision, we accepted TransGrid's proposed weighted average method to calculate the remaining tax asset lives as at 1 July 2014. We noted that the remaining tax asset lives would be updated for the final decision because TransGrid's revised proposal would include revisions for 2013–14 actual capex. This is because the   
   2013–14 capex values are used to calculate the weighted average remaining tax asset lives in the RFM. Based on the further change to the 2013–14 capex as discussed in section 8.4.1 we have updated the remaining tax asset lives as at 1 July 2014 for this final decision.
2. We are satisfied the proposed standard and remaining tax asset lives are likely to provide an appropriate estimate of the tax depreciation amount for a benchmark efficient TNSP as required by the NER.[[6]](#footnote-6)
3. Table 8‑4 sets out our final decision on the standard and remaining tax asset lives as at 1 July 2014 for TransGrid.

Table 8‑4 AER's final decision on TransGrid's standard and remaining tax asset lives as at 1 July 2014 (years)

| Asset class | Standard tax asset life | Remaining tax asset life as at  1 July 2014 |
| --- | --- | --- |
| Transmission lines (pre 2004-05) | n/a | 2.1 |
| Underground cables (pre 2004-05) | n/a | 34.6 |
| Substations including buildings (pre 2004-05) | n/a | 12.2 |
| SCADA and communications (pre 2004-05) | n/a | 0.4 |
| Non-network assets (pre 2004-05) | n/a | n/a |
| SMHEA assets (pre 2004-05) | n/a | n/a |
| Transmission lines (2004-09) | n/a | 44.1 |
| Underground cables (2004-09) | n/a | 36.4 |
| Substations including buildings (2004-09) | n/a | 33.8 |
| SCADA and communications (2004-09) | n/a | 8.8 |
| Non-network assets (2004-09) | n/a | 3.5 |
| Transmission lines & cables (2009-14) | n/a | 48.7 |
| Substations (2009-14) | n/a | 38.2 |
| Secondary systems (2009-14) | n/a | 33.5 |
| Communications (2009-14) | n/a | 33.4 |
| Business IT (2009-14) | n/a | 3.0 |
| Minor plant, motor vehicles & mobile plant (2009-14) | n/a | 6.2 |
| Equity raising costs (2009-14) | n/a | 36.6 |
| Transmission lines (2014-18) | 50.0 | n/a |
| Underground cables (2014-18) | 45.0 | n/a |
| Substations (2014-18) | 40.0 | n/a |
| Secondary systems (2014-18) | 15.0 | n/a |
| Communications (short life) (2014-18)a | 10.0 | n/a |
| Business IT (2014-18) | 4.0 | n/a |
| Minor plant, motor vehicles & mobile plant (2014-18) | 8.0 | n/a |
| Transmission line life extension (2014-18) | 25.0 | n/a |
| Equity raising costs (2014-18)b | n/a | n/a |
| Land and easements | n/a | n/a |

Source: AER analysis.

n/a: Not applicable. The asset classes ending with '(pre 2004-05)'; '(2004-09)'; and '(2009-14)' do not have assigned standard tax asset lives because forecast capex is no longer allocated to them.

(a) As discussed in our draft decision attachment 5, we have changed the name of this asset class to 'Communications (short life) 2014–18' to better reflect the nature of the assets allocated to this asset class.

(b) For this final decision, TransGrid does not satisfy the requirements to incur benchmark equity raising costs associated with its forecast capex for the 2014–18 period. Therefore, a standard tax asset life for equity raising costs (2014–18) is not required.

1. NER, cl. 6A.5.4(a)(4). [↑](#footnote-ref-1)
2. TransGrid, Revised revenue proposal, p.130; TransGrid, Revised proposed PTRM, January 2015. [↑](#footnote-ref-2)
3. NER, cl. 6A.6.4. [↑](#footnote-ref-3)
4. AER, TransGrid 2015-18 draft transmission determination, November 2014, Attachment 8. [↑](#footnote-ref-4)
5. TransGrid, Email response to information request by AER, 27 January 2015. [↑](#footnote-ref-5)
6. NER, cl. 6A.6.4. [↑](#footnote-ref-6)