



FINAL DECISION
ActewAGL Distribution
Access Arrangement
2016 to 2021

Attachment 8 – Corporate
income tax

May 2016

© Commonwealth of Australia 2016

This work is copyright. In addition to any use permitted under the Copyright Act 1968, all material contained within this work is provided under a Creative Commons Attributions 3.0 Australia licence, with the exception of:

- the Commonwealth Coat of Arms
- the ACCC and AER logos
- any illustration, diagram, photograph or graphic over which the Australian Competition and Consumer Commission does not hold copyright, but which may be part of or contained within this publication. The details of the relevant licence conditions are available on the Creative Commons website, as is the full legal code for the CC BY 3.0 AU licence.

Requests and inquiries concerning reproduction and rights should be addressed to the:

Director, Corporate Communications
Australian Competition and Consumer Commission
GPO Box 4141, Canberra ACT 2601

or publishing.unit@acc.gov.au.

Inquiries about this publication should be addressed to:

Australian Energy Regulator
GPO Box 520
Melbourne Vic 3001

Tel: (03) 9290 1444

Fax: (03) 9290 1457

Email: AERInquiry@aer.gov.au

Note

This attachment forms part of the AER's final decision on the access arrangement for ActewAGL Distribution for 2016–21. It should be read with all other parts of the final decision.

The final decision includes the following documents:

Overview

Attachment 1 - Services covered by the access arrangement

Attachment 2 - Capital 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 carryover mechanism

Attachment 10 - Reference tariff setting

Attachment 11 - Reference tariff variation mechanism

Attachment 12 - Non-tariff components

Attachment 13 - Demand

Contents

Note	8-2
Contents	8-3
Shortened forms	8-4
8 Corporate income tax.....	8-6
8.1 Final decision.....	8-6
8.2 ActewAGL’s revised proposal.....	8-7
8.3 AER’s assessment approach.....	8-8
8.4 Reasons for final decision	8-9
8.4.1 Opening tax asset base as at 1 July 2015.....	8-9
8.4.2 Standard tax asset lives	8-10
8.4.3 Remaining tax asset lives as at 1 July 2015.....	8-11

Shortened forms

Shortened form	Extended form
AA	Access Arrangement
AAI	Access Arrangement Information
AER	Australian Energy Regulator
ASA	Asset Services Agreement
ATO	Australian Tax Office
capex	capital expenditure
CAPM	capital asset pricing model
CCP	Consumer Challenge Panel
CMF	construction management fee
CPI	consumer price index
DAMS	Distribution Asset Management Services
DRP	debt risk premium
EBSS	Efficiency Benefit Sharing Scheme
ECM	Efficiency Carryover Mechanism
EIL	Energy Industry Levy
ERP	equity risk premium
Expenditure Guideline	Expenditure Forecast Assessment Guideline
gamma	value of imputation credits
GSL	Guaranteed Service Level
GTA	Gas Transport Services Agreement
ICRC	Independent Competition and Regulatory Commission
MRP	market risk premium
NECF	National Energy Customer Framework
NERL	National Energy Retail Law
NERR	National Energy Retail Rules
NGL	National Gas Law
NGO	National Gas Objective
NGR	National Gas Rules
NPV	net present value
opex	operating expenditure

Shortened form	Extended form
PFP	partial factor productivity
PPI	partial performance indicators
PTRM	post-tax revenue model
RBA	Reserve Bank of Australia
RFM	roll forward model
RIN	regulatory information notice
RoLR	retailer of last resort
RSA	Reference Service Agreement
RPP	revenue and pricing principles
SLCAPM	Sharpe-Lintner capital asset pricing model
STTM	Short Term Trading Market
TAB	tax asset base
UAFG	unaccounted for gas
UNFT	Utilities Network Facilities Tax
WACC	weighted average cost of capital
WPI	Wage Price Index

8 Corporate income tax

When determining the total revenue for ActewAGL, we must estimate ActewAGL's cost of corporate income tax.¹ ActewAGL has adopted the post-tax framework to derive its revenue requirement for 2015–16 and the 2016–21 access arrangement period.² Under the post-tax framework, a separate corporate income tax allowance is calculated as part of the building blocks assessment.

8.1 Final decision

We do not approve ActewAGL's revised proposed cost of corporate income tax of \$20.0 million (\$nominal) for 2015–16 and the 2016–21 access arrangement period. This is mainly a consequence of our adjustments to ActewAGL's proposed value of imputation credits–gamma–(attachment 4) and other building block costs that affect revenues, such as the rate of return on capital (attachment 3), forecast capex (attachment 6) and forecast opex (attachment 7).³

Consistent with our draft decision, we accept ActewAGL's proposed method to roll forward the tax asset base (TAB) because it is consistent with the AER's roll forward model (RFM) for electricity service providers and the approach previously approved in gas access arrangement decisions. In accepting the approach, however, we have updated ActewAGL's opening TAB as at 1 July 2015 to \$231.7 million (\$nominal) to reflect ActewAGL's updated revised conforming capex for 2014–15 as discussed in attachment 2. Our final decision is 0.3 million or 0.1 per cent (\$nominal) higher than ActewAGL's revised proposed value of \$231.4 million (\$nominal).

Our adjustments result in an estimated cost of corporate income tax of \$9.4 million (\$nominal) for ActewAGL for 2015–16 and the 2016–21 access arrangement period as shown in table 8.1.

We have revised the access arrangement having regard to our reasons for refusing to approve ActewAGL's proposal and the further matters identified in the NGR section 64(2). Our revisions are reflected in the *Approved Access Arrangement for ACT, Queanbeyan and Palerang gas distribution network 2016–2021*, which gives effect to this decision.

¹ NGR, r. 76(c).

² ActewAGL, *Response to the AER's draft decision - 2016–21 ACT, Queanbeyan and Palerang access arrangement*, January 2016 p. 30.

³ Changes to other building block costs affect revenues, which also impact the tax calculation.

Table 8.1 AER’s final decision on cost of corporate income tax for ActewAGL for 2015–16 and the 2016–21 access arrangement period (\$million, nominal)

	2015–16	2016–17	2017–18	2018–19	2019–20	2020–21	Total
Tax payable	1.5	1.8	2.6	3.1	3.3	3.4	15.6
Less: value of imputation credits	0.6	0.7	1.0	1.2	1.3	1.4	6.2
Net corporate income tax allowance	0.9	1.1	1.5	1.9	2.0	2.0	9.4

Source: AER analysis.

8.2 ActewAGL’s revised proposal

ActewAGL's revised proposal forecast a cost of corporate income tax of \$20.0 million (\$nominal) for 2015–16 and the 2016–21 access arrangement period. ActewAGL's methodology for determining its cost of corporate income tax is unchanged from its initial proposal.

ActewAGL adopted the methodology accepted in our draft decision to determine the revised proposed tax asset base (TAB) at 1 July 2015. The TAB was updated for 2014–15 actual capex.

ActewAGL’s revised proposed roll forward of its TAB over the 2010–15 access arrangement period is set out in Table 8.2.

Table 8.2 ActewAGL’s revised proposed tax asset base roll forward over the 2010–15 access arrangement period (\$million, nominal)

	2010–11	2011–12	2012–13	2013–14	2014–15
Opening tax asset base	191.6	195.8	201.0	210.9	218.7
Capex	12.8	14.3	19.4	17.8	23.2
Tax depreciation	–8.6	–9.1	–9.5	–10.0	–10.5
Closing tax asset base	195.8	201.0	210.9	218.7	231.4

Source: ActewAGL, *Revised proposed RFM*, January 2016.

Applying the same approach accepted in the draft decision, ActewAGL's revised proposal calculated the corporate income tax over 2015–16 and the 2016–21 access arrangement period using the following inputs:⁴

- Revised opening TAB of \$231.4 million (\$nominal) as at 1 July 2015, reflecting updates for 2014–15 actual capex.
- An expected statutory income tax rate of 30 per cent per year.
- A value for the assumed utilisation of imputation credits (gamma) of 0.25 which is consistent with its initial proposal.
- The standard tax asset lives as approved for the 2010–15 access arrangement period.
- Revised remaining tax asset lives as at 1 July 2015 which are calculated using a weighted average remaining life approach as contained in its revised proposed RFM.
- Revised forecast capex.
- Revised forecast opex.

ActewAGL's revised proposed cost of corporate income tax for 2015–16 and the 2016–21 access arrangement period is \$20.0 million (\$nominal) as set out in Table 8.3.

Table 8.3 ActewAGL's revised proposed corporate income tax allowance for 2015–16 and the 2016–21 access arrangement period (\$million, nominal)

	2015–16	2016–17	2017–18	2018–19	2019–20	2020–21	Total
Tax payable	3.0	3.5	4.4	5.0	5.3	5.5	26.7
Less: value of imputation credits	0.7	0.9	1.1	1.3	1.3	1.4	6.7
Net corporate income tax allowance	2.2	2.6	3.3	3.8	4.0	4.1	20.0

Source: ActewAGL, *Revised proposed PTRM*, January 2016.

8.3 AER's assessment approach

We have not changed our assessment approach for the corporate income tax from our draft decision. Section 8.3 of our draft decision details that approach.⁵

⁴ ActewAGL, *Response to the AER's draft decision - 2016–21 ACT, Queanbeyan and Palerang access arrangement*, January 2016 p. 91.

⁵ AER, *Draft decision: ActewAGL Distribution access arrangement 2016–21, attachment 8*, November 2015, pp. 8–11.

8.4 Reasons for final decision

Our final decision on ActewAGL's corporate income tax allowance is \$9.4 million (\$nominal), which is a reduction of \$10.6 million (\$nominal) or 53.2 per cent of ActewAGL's revised proposal.

Consistent with our draft decision, we accept ActewAGL's proposed approach for calculating the corporate income tax allowance. In accepting the approach we have adjusted several inputs to ActewAGL's revised proposed PTRM for calculating the corporate income tax allowance. These relate to:

- Changing the value of gamma to 0.4 from 0.25 (attachment 4).
- Changes to other building block components including the rate of return on capital (attachment 3), forecast capex (attachment 6) and opex (attachment 7) that impact total revenues and therefore also impact the forecast corporate income tax allowance.⁶

8.4.1 Opening tax asset base as at 1 July 2015

Consistent with the draft decision, we accept ActewAGL's proposed method to roll forward the TAB. In accepting the approach, however, we have updated ActewAGL's opening TAB as at 1 July 2015 to \$231.7 million, which is 0.3 million or 0.1 per cent (\$nominal) higher than ActewAGL's revised proposed value of \$231.4 million (\$nominal). This is because ActewAGL updated its revised proposed conforming capex for 2014–15. As discussed in attachment 2, we accept ActewAGL's updated revised capex for 2014–15 as conforming capex. Our amendment to ActewAGL's revised proposed opening TAB reflects this updated value. For this final decision we are satisfied the actual capex for 2014–15 included in the TAB reflects the requirements of r. 79 of the NGR. Our detailed assessment of conforming capex for the 2010–15 access arrangement period is set out in attachment 6.

Table 8.4 sets out our final decision on the roll forward of ActewAGL's TAB values.

⁶ NGR, r. 87A.

Table 8.4 AER’s final decision on ActewAGL’s tax asset base roll forward for the 2010–15 access arrangement period (\$million, nominal)

	2010–11	2011–12	2012–13	2013–14	2014–15
Opening tax asset base	191.6 ^a	195.8	201.0	210.9	218.7
Capex	12.8	14.3	19.4	17.8	23.5
Tax depreciation	–8.6	–9.1	–9.5	–10.0	–10.5
Closing tax asset base	195.8	201.0	210.9	218.7	231.7

Source: AER analysis.

(a) The approved opening TAB as at 1 July 2010 has been adjusted for the difference between the actual and forecast capex for 2009–10.

8.4.2 Standard tax asset lives

Consistent with our draft decision, we approve ActewAGL’s proposed standard tax asset lives assigned to each of its asset classes for 2015–16 and the 2016–21 access arrangement period. This is because they are consistent with the statutory cap on the effective life of gas transmission assets under the *Income Tax Assessment Act (ITAA) 1997*, and with the standard tax asset lives prescribed in the Tax Ruling 2015/2.⁷ The revised proposed standard tax asset lives are also consistent with the approved standard tax asset lives in the 2010–15 access arrangement.⁸

In our draft decision we created a ‘Land and easement’ asset class for ActewAGL’s forecast land capex in 2015–16 and the 2016–21 access arrangement period.⁹ We did not apply a standard tax asset life to this new asset class for tax depreciation purposes (“n/a” is assigned for tax depreciation modelling purposes in the PTRM). This is because land and easement are non-depreciating assets, and therefore should not have a standard tax asset life for tax depreciation purposes. This approach is consistent with Australian accounting standards and ATO’s treatment for such assets.¹⁰ ActewAGL’s revised proposal adopted our draft decision on the ‘Land and easement’ asset class.¹¹

Table 8.5 sets out our final decision on the standard tax asset lives for ActewAGL.

⁷ ITAA 1997, s. 40.102(5); Australian Taxation Office, *Taxation Ruling Income tax: effective life of depreciating assets (applicable from 1 July 2015)*: <http://law.ato.gov.au/atolaw/view.htm?docid=%22TXR%2FTR20152%2FNAT%2FATO%2F00001%22>.

⁸ AER, *Final decision PTRM for ActewAGL (Tribunal varied)*, June 2010.

⁹ AER, *Draft decision, attachment 8*, November 2015, p.6.

¹⁰ Australian accounting standard board, *Accounting standard AASB1021: Depreciation, August 1997*, pp. 10–11; ATO, *Guide to depreciating assets 2011*, 2011, p. 3.

¹¹ ActewAGL, *Response to the AER’s draft decision: 2016–21 Queanbeyan and Palerang Gas Network Access Arrangement*, January 2016. p. 91.

8.4.3 Remaining tax asset lives as at 1 July 2015

Consistent with our draft decision, we accept ActewAGL's proposed weighted average method to calculate the remaining tax asset lives as at 1 July 2015. In accepting the weighted average method, we have updated ActewAGL's remaining tax asset lives as at 1 July 2015 for this final decision.

In the draft decision, we changed some formulae in the tax asset lives roll forward calculation in ActewAGL's RFM to incorporate 2009–10 actual capex. We noted that the remaining tax asset lives would be updated for the final decision because ActewAGL's revised proposal would include revisions for 2014–15 actual capex. This is because the capex is used as an input to calculate the weighted average remaining tax asset lives.

We note that ActewAGL's revised proposal adopted our draft decision changes to some formulae in the tax asset lives roll forward. It also corrected an error in its RFM for the reported allocation of actual capex between the 'contract meters' and 'tariff meters' asset class, which causes a minor change to the remaining tax asset lives from the draft decision. We accept this change as this is for correcting a previous error in the RFM.

Also, as discussed in section 8.4.1, ActewAGL has updated its revised proposed actual capex for 2014–15 and we have accepted the updated value as conforming capex. Our amendment to ActewAGL's revised proposed remaining tax asset lives reflects the conforming capex for 2014–15.

Our final decision on ActewAGL's standard tax asset lives and remaining tax asset lives for each of its asset classes for 2015–16 and the 2016–21 access arrangement period is set out in Table 8.5.

Table 8.5 AER’s final decision on ActewAGL’s standard tax asset lives and remaining tax asset lives as at 1 July 2015 for 2015–16 and the 2016–21 access arrangement period (years)

Tax asset class	Standard tax asset life	Remaining tax asset life as at 1 July 2015
HP mains	50	42.6
HP services	50	29.4
MP mains	50	29.5
MP services	30	24.9
TRS and DRS—valves and regulators	40	38.3
Contract meters	15	2.4
Tariff meters	15	13.2
Regulatory costs	5	n/a
IT system ^a	5	1.0
Land and easement	n/a	n/a

Source: AER analysis.

(a) The remaining tax asset life as at 1 July 2015 for the ‘IT system’ asset class is set to one year in order to fully depreciate the small residual TAB value for this asset class within 2015–16 and the 2016–21 access arrangement period.

n/a Not applicable.