FINAL DECISION
AusNet Services distribution determination 2016 to 2020

Attachment 8 – Corporate income tax

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Note

This attachment forms part of the AER's final decision on AusNet Services' distribution determination for 2016–20. It should be read with all other parts of the final decision.

The final 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

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Contents

Shortened forms

Shortened form	Extended form
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
AMI	Advanced metering infrastructure
Augex	augmentation expenditure
Capex	capital expenditure
CCP	Consumer Challenge Panel
CESS	capital expenditure sharing scheme
CPI	consumer price index
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
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

Shortened form	Extended form
Repex	replacement expenditure
RFM	roll forward model
RIN	regulatory information notice
RPP	revenue and 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 AusNet Services' 2016–20 regulatory control 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 AusNet Services to recover the costs associated with the estimated corporate income tax payable during the 2016–20 regulatory control period.

This attachment presents our final decision on AusNet Services' revised proposed corporate income tax allowance for the 2016–20 regulatory control period. It also presents our final decision on its 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.

8.1 Final decision

We do not accept AusNet Services' revised proposed cost of corporate income tax allowance of $254.7 million ($ nominal).[2] Our final decision on the estimated cost of corporate income tax is $143.7 million ($ nominal) for AusNet Services over the 2016–20 regulatory control period. This represents a reduction of $110.9 million (or 43.6 per cent) from its revised proposal.

The reduction reflects our amendments to AusNet's proposed inputs for forecasting the cost of corporate income tax such as the opening TAB (section 8.4.1) and the value of imputation credits—gamma—(attachment 4). Changes to the building block costs also affect revenues, which in turn impacts the tax calculation. The changes affecting revenues are discussed in attachment 1.

Table 8.1 sets out our final decision on the estimated cost of corporate income tax allowance for AusNet Services over the 2016–20 regulatory control period.

Table 8.1 AER's final decision on AusNet Services' cost of corporate income tax allowance for the 2016–20 regulatory control period ($ million, nominal)

	2016	2017	2018	2019	2020	Total
Tax payable	55.4	45.1	46.0	47.2	45.8	239.5
Less: value of imputation credits	22.2	18.0	18.4	18.9	18.3	95.8
Net corporate income tax allowance	**33.2**	**27.1**	**27.6**	**28.3**	**27.5**	**143.7**

Source: AER analysis.

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

[2] AusNet Services, *Revised regulatory proposal*, January 2015, p.10–2.

8.2 AusNet Services' revised proposal

AusNet Services' revised proposal forecasts a cost of corporate income tax allowance of $254.7 million ($ nominal) for the 2016–20 regulatory control period. AusNet Services' revised proposal adopted the methodology approved in the preliminary decision for determining its corporate income tax.

AusNet Services has revised its corporate income tax allowance using the AER's PTRM and included the following inputs:

- revised forecast capex
- revised forecast opex.

AusNet Services' revised proposal also used the opening TAB at 1 January 2016, standard and remaining tax asset lives consistent with those approved in the preliminary decision. However, it used a value for gamma of 0.25 consistent with its initial proposal.

Table 8.2 sets out AusNet Services' revised proposed corporate income tax allowance for the 2016–20 regulatory control period.

Table 8.2 AusNet Services' proposed cost of corporate income tax allowance for the 2015–20 regulatory control period ($ million, nominal)

	2016	2017	2018	2019	2020	Total
Tax payable	73.5	63.6	65.9	68.4	68.2	339.5
Less: value of imputation credits	18.4	15.9	16.5	17.1	17.0	84.9
Net corporate income tax allowance	**55.1**	**47.7**	**49.4**	**51.3**	**51.1**	**254.7**

Source: AusNet Services, *Revised regulatory proposal*, January 2016, p. 10–6.

8.3 Assessment approach

We have not changed our assessment approach for the cost of corporate income tax from our preliminary decision. Section 8.3 of our preliminary decision details that approach.[3]

8.4 Reasons for final decision

We do not accept AusNet Services' revised proposed cost of corporate income tax allowance of $254.7 million ($ nominal). We instead determine a cost of corporate income tax allowance of $143.7 million for the 2016–20 regulatory control period. This

3 AER, *Preliminary decision, AusNet Services determination 2015–16 to 2019–20: Attachment 8 – Corporate income tax*, April 2015, pp. 7–10.

represents a reduction of $110.9 million (or 43.6 per cent) from AusNet Services' revised proposal.

This is because we adjusted the following proposed inputs to the PTRM for tax purposes:

- the value of gamma (attachment 4)
- other building block components including forecast opex (attachment 7) and forecast capex (attachment 6) that affect revenues, and therefore also impact the forecast corporate income tax allowance.

We accept the revised proposed opening tax asset base (section 8.4.1), remaining tax asset lives (section 8.4.2) and the standard tax asset lives (section 8.4.3), consistent with those approved in the preliminary decision.

8.4.1 Opening tax asset base

We accept AusNet Services' proposed opening TAB value at 1 January 2016 of $2218.2 million ($ nominal). This is the same amount approved in the preliminary decision.

In the preliminary decision, we accepted AusNet Services' proposed method to establish the opening TAB at 1 January 2016 as it was based on the approach approved at the 2010 determination. However, we amended AusNet Services' proposed opening TAB by removing the transfer of $47.3 million at 1 January 2016 for AMI IT and communication assets from alternative control services to standard control services. AusNet Services' revised proposal adopted our draft decision amendment.

We noted the roll forward of AusNet Services' TAB included an estimated capex value for 2015. We stated we would update the 2015 estimated capex value for the final decision. AusNet's revised proposal did not include an update for 2015 estimated capex. In response to an information request, AusNet Services advised that it has encountered a data migration issue arising from upgrades to its IT systems.[4] For the reasons discussed in attachment 2, we accept that the estimate approved in the preliminary decision should continue to serve as the best estimate for this final decision. We will update the TAB for 2015 actual capex at the next reset.

Table 8.3 sets out our final decision on the roll forward of AusNet Services' TAB values over the 2011–15 regulatory control period.

[4] AusNet Services, *RE: AER information request – Jemena - #030 – 2015 estimated capex update*, 8 February 2016.

Table 8.3 AER's final decision on AusNet Services' TAB roll forward ($ million, nominal)

	2011	2012	2013	2014	2015[a]
Opening TAB	1278.7	1444.8	1624.3	1832.8	2041.0
Capital expenditure	290.8	331.1	386.3	428.2	387.4
Less: Tax depreciation	124.8	151.5	177.8	220.0	210.2
Closing TAB	**1444.8**	**1624.3**	**1832.8**	**2041.0**	**2218.2**

Source: AER analysis.

(a) Based on estimated capex.

8.4.2 Remaining tax asset lives

We accept AusNet Services' revised proposed remaining tax asset lives calculated based on the approach approved in our preliminary decision. The approach calculates the remaining tax asset life for each asset class at 1 January 2016 using the standard tax asset life for that asset class multiplied by the ratio of the RAB remaining asset life to the RAB standard asset life.

In the preliminary decision, we accepted AusNet Services' proposal to transition to our preferred straight-line tax depreciation approach to calculate the corporate income tax allowance for the 2016–20 regulatory control period. This required us to determine remaining tax asset lives for depreciating the opening TAB at 1 January 2016. We considered AusNet Services' proposed approach to determine remaining tax asset lives provides reasonable estimates for the majority of its asset classes.

We noted the remaining tax asset lives at 1 January 2016 may be updated using the approved approach for any revision to the RAB remaining asset lives, which in turn depends on any changes in 2015 capex. For the reasons discussed in attachment 2, we have not made any further changes to the 2015 capex estimate for this final decision. Therefore, our final decision on the remaining tax asset lives for AusNet Services remains the same as those in the preliminary decision.

We are satisfied the remaining tax asset lives in AusNet Services' revised proposal are likely to provide an appropriate estimate of the tax depreciation amount for a benchmark efficient service provider as required by the NER.[5]

Table 8.4 sets out our final decision on the remaining tax asset lives at 1 January 2016 for AusNet Services.

[5] NER, cl. 6.5.3.

8.4.3 Standard tax asset lives

Consistent with our preliminary decision, we accept AusNet Services' proposed standard tax asset lives because they are:

- broadly consistent with the values prescribed by the Commissioner for taxation in tax ruling 2015/2[6]
- the same as the approved standard tax asset lives for the 2011–15 regulatory control period.

In the preliminary decision, we considered that the opening TAB value for land as at 1 January 2016 should be allocated to its own asset class as land assets do not depreciate. We therefore created a new non-depreciating 'Land' asset class. AusNet Services' revised proposal adopted our preliminary decision to create a new 'Land' asset class with no standard life assigned to it.

We are satisfied the standard tax asset lives in AusNet Services' revised proposal are likely to provide an appropriate estimate of the tax depreciation amount for a benchmark efficient service provider as required by the NER.[7]

Table 8.4 sets out our final decision on the standard tax asset lives for AusNet Services.

6 ATO, *Taxation Ruling Income tax: effective life of depreciating assets (applicable from 1 July 2015)*, July 2015, http://law.ato.gov.au/atolaw/view.htm?docid=%22TXR%2FTR20152%2FNAT%2FATO%2F00001%22, accessed on 9 March 2016.

7 NER, cl. 6.5.3.

Table 8.4 AER's final decision on AusNet Services' standard tax asset lives (years)

Asset class	Standard tax asset life	Remaining tax asset life as at 1 January 2016
Subtransmission	43.0	34.0
Distribution system assets	46.0	31.7
Standard metering	n/a	1.0[a]
Public lighting	n/a	n/a
SCADA/Network control	10.0	6.9
Non-network general assets - IT	4.0	2.6
Non-network general - Other	12.0	8.3
Land	n/a	n/a
Accelerated depreciation opening RAB adjustment - Subtransmission	n/a	n/a
Accelerated depreciation opening RAB adjustment - Distribution	n/a	n/a
Accelerated depreciation - Subtransmission (2016–20)	n/a	n/a
Accelerated depreciation - Distribution (2016–20)	n/a	n/a
Equity raising costs	5.0	n/a

Source: AER analysis.

n/a not applicable.

a: The remaining tax asset life as at 1 January 2016 for the 'Standard metering' asset class is set to 1 year in order to fully depreciate the small residual TAB value for this asset class within the 2016–20 regulatory control period.

8.4.4 Tax treatment of other revenue adjustments

We note AusNet Services' revised proposal adopted our preliminary decision on the tax treatment of the revenue adjustments arising from the operation of the EBSS over the 2011–15 regulatory control period and the close out of the ESCV's previous S-factor scheme.[8] Consistent with the preliminary decision, our final decision is that the EBSS and S-factor revenue adjustments should be given identical income and expense tax status in the PTRM.[9]

8 AusNet Services, *Revised regulatory proposal*, January 2016, p. 2-11.

9 That is, the revenue adjustments are either both tax income and tax expense (EBSS, shared assets); or neither tax income nor tax expense (S-factor).