FINAL DECISION
SA Power Networks determination 2015−16 to 2019−20

Attachment 8 − Corporate income tax

October 2015

AUSTRALIAN ENERGY REGULATOR

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 SA Power Networks' 2015–20 distribution determination. 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

Attachment 7 – Operating expenditure

Attachment 8 – Corporate income tax

Attachment 9 – Efficiency benefit sharing scheme

Attachment 10 – Capital expenditure sharing scheme

Attachment 11 – Service target performance incentive scheme

Attachment 12 – Demand management incentive scheme

Attachment 13 – Classification of services

Attachment 14 – Control mechanism

Attachment 15 – Pass through events

Attachment 16 – Alternative control services

Attachment 17 – Negotiated services framework and criteria

Attachment 18 – Connection policy

Contents

Shortened forms

Shortened form	Extended form
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
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

Shortened form	Extended form
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 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 SA Power Networks' 2015–20 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 SA Power Networks to recover the costs associated with the estimated corporate income tax payable during the 2015–20 regulatory control period.

This attachment presents our final decision on SA Power Networks' revised proposed corporate income tax allowance for the 2015–20 regulatory control period. It also presents our final decision on its revised proposed opening tax asset base (TAB), the standard tax asset lives for depreciating capex and revised proposed depreciation approach for existing tax assets. The estimated tax depreciation is used for the purpose of calculating tax expenses.

8.1 Final decision

We do not accept SA Power Networks' revised proposed cost of corporate income tax allowance of $426.5 million ($ nominal). Our final decision on the estimated cost of corporate income tax is $258.3 million ($ nominal) for SA Power Networks over the 2015–20 regulatory control period. This represents a reduction of $168.2 million (or 39.4 per cent) from its revised proposal.

The reduction reflects our amendment to one of SA Power Networks' revised proposed inputs for forecasting the cost of corporate income tax. This is due to some changes to the implementation of its revised proposed tax depreciation approach for existing tax assets, which we accept (section 8.4.2). The reduction also reflects our final decision on 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 SA Power Networks over the 2015–20 regulatory control period.

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

Table 8.1 AER's final decision on SA Power Networks' cost of corporate income tax allowance for the 2015–20 regulatory control period ($ million, nominal)

	2015–16	2016–17	2017–18	2018–19	2019–20	Total
Tax payable	64.8	87.4	86.5	90.9	101.0	430.6
Less: value of imputation credits	25.9	34.9	34.6	36.4	40.4	172.2
Net corporate income tax allowance	**38.9**	**52.4**	**51.9**	**54.5**	**60.6**	**258.3**

Source: AER analysis.

8.2 SA Power Networks' revised proposal

SA Power Networks' revised proposal forecasts a cost of corporate income tax allowance of $426.5 million ($ nominal) for the 2015–20 regulatory control period. SA Power Networks' methodology for determining its corporate income tax is unchanged from its initial proposal. We accepted the approach in our preliminary decision.

SA Power Networks has revised its corporate income tax allowance using our PTRM and included the following inputs:[2]

- a revised opening TAB as at 1 July 2015 of $2485.4 million ($ nominal), reflecting updates for 2014–15 estimated capex and input correction for 2009–10 customer contributions
- remaining asset lives based on a revised approach to determining tax depreciation of existing tax assets. This revised approach provides for tax depreciation of capex for each year of a regulatory control period individually, and is the same as the revised approach applying to its regulatory depreciation
- revised forecast capex
- revised forecast opex.

SA Power Networks also used the standard 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 SA Power Networks' revised proposed corporate income tax allowance for the 2015–20 regulatory control period.

2 SA Power Networks, *Revised regulatory proposal*, July 2015, pp. 414–415.

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

	2015–16	2016–17	2017–18	2018–19	2019–20	Total
Tax payable	106.8	109.1	112.7	117.7	122.4	568.7
Less: value of imputation credits	26.7	27.3	28.2	29.4	30.6	142.2
Net corporate income tax allowance	**80.1**	**81.8**	**84.6**	**88.3**	**91.8**	**426.5**

Source: SA Power Networks, *Revised regulatory proposal*, July 2015, p. 415 and attachment P.1.

8.3 AER's 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 SA Power Networks' revised proposed cost of corporate income tax allowance of $426.5 million ($ nominal). We instead determine a cost of corporate income tax allowance of $258.3 million for the 2015–20 regulatory control period. This represents a reduction of $168.2 million (or 39.4 per cent) from SA Power Networks' revised proposal.

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

- forecast tax depreciation for existing tax assets at 1 July 2015 (section 8.4.2)
- 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 standard tax asset lives consistent with those approved in the preliminary decision (section 8.4.3).

8.4.1 Opening tax asset base

We accept SA Power Networks' proposed opening TAB value at 1 July 2015 of $2485.4 million ($ nominal).

[3] AER, *Preliminary decision, SA Power Networks determination 2015–16 to 2019–20: Attachment 8 – Corporate income tax*, April 2015, pp. 7–10.

In the preliminary decision, we accepted SA Power Networks' proposed opening TAB after being satisfied that it had correctly made all relevant inputs to the roll forward model (RFM). We noted the roll forward of SA Power Networks' TAB included an estimated capex value for 2014–15. We stated we would update the 2014–15 estimated capex value for the final decision.

SA Power Networks' revised proposed opening TAB at 1 July 2015 is calculated based on the method accepted in our preliminary decision, with updates for 2014–15 capex. The only change proposed by SA Power Networks is to allocate the input for 2009–10 customer contributions as a negative capex amount under the actual capex section of the RFM instead of a positive entry under the customer contribution section.[4]

For the reasons discussed in attachment 2, we accept SA Power Networks' update to the net capex estimate for 2014–15 of $335.4 million.[5] This amount is lower than in the initial proposal and reflects more up-to-date data, and therefore is the best forecast available. We note that the difference between actual and estimated capex for 2014–15 will be accounted for at the next reset. We also accept SA Power Networks' re-allocation of the input for 2009–10 customer contributions ($152.5 million) under the actual capex section of the RFM rather than under the customer contribution section. We are satisfied that this input correction is consistent with the tax roll forward method for establishing the TAB approved in the 2010 determination.[6]

Table 8.3 sets out our final decision on the roll forward of SA Power Networks' TAB values over the 2010–15 regulatory control period. The closing TAB for 2014–15 becomes the opening TAB as at 1 July 2015.

Table 8.3 AER's final decision on SA Power Networks' TAB roll forward ($ million, nominal)

	2010–11	2011–12	2012–13	2013–14	2014–15[b]
Opening TAB	1039.7	1344.7	1675.2	1973.2	2223.3
Capital expenditure[a]	367.4	403.5	391.9	360.2	391.6
Less: Tax depreciation	62.4	73.0	93.9	110.2	129.4
Closing TAB	1344.7	1675.2	1973.2	2223.3	2485.4

Source: AER analysis.

(a) Net of disposals.

(b) Based on estimated capex.

4 SA Power Networks, *Revised regulatory proposal*, July 2015, attachment L.1.

5 The net capex amount for the TAB roll forward is calculated as actual gross capex less asset disposals. This is different from the net capex amount used to roll forward the RAB because for TAB purposes, net capex includes customer contributions and excludes the half-WACC adjustment.
The 2014–15 net capex for TAB roll forward is $473.0 million ($nominal).

6 AER, *Final decision, South Australia distribution determination 2010–11 to 2014–15*, May 2010, pp. 162–163; and Roll forward model.

8.4.2 Remaining tax asset lives

SA Power Networks has proposed a different approach to determining remaining tax asset lives and depreciation associated with existing tax assets than the approach set out in its initial proposal.[7] The revised approach is the same as outlined in attachment 5 for depreciating existing assets in the RAB. Under this approach, the capex for each year of a regulatory control period will be depreciated individually for tax purposes.

Consistent with our decision for SA Power Networks' revised regulatory depreciation approach, we accept the revised tax depreciation approach proposed by SA Power Networks. For the same reasons as discussed in attachment 5, the revised approach will result in each tax asset class having an expanding list of sub-assets to reflect the regulatory year in which capital expenditures on those assets occurred.[8] This extra data helps track remaining tax asset values and associated tax depreciation, and is therefore consistent with the NER. However, we have made some changes to SA Power Networks' implementation of the approach for clarity and to prevent a distortion in the tax depreciation profile. Section 5.4.2 of attachment 5 explains the method and implementation in greater detail.

With our changes, we are satisfied the revised approach provides an estimate of the tax depreciation amount for a benchmark efficient service provider as required by the NER.[9]

8.4.3 Standard tax asset lives

Consistent with our preliminary decision, we accept SA Power Networks' proposed standard tax asset lives because they are:

- broadly consistent with the values prescribed by the Commissioner for taxation in tax ruling 2014/4[10]
- the same as the approved standard tax asset lives for the 2010–15 regulatory control period.

We are satisfied the standard tax asset lives in SA Power Networks' 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.[11]

---

7 SA Power Networks, *Revised regulatory proposal*, July 2015, p. 414.

8 SA Power Networks prepared a model (SA Power NetworksN.2_PUBLIC_Reg Asset Register –SCS) where the individual calculations of tax depreciation occur. However, it still presented in the PTRM only a single remaining tax asset life for existing assets as at 1 July 2015. This causes minor implementation issues this period and is discussed further in attachment 5.

9 NER, cl. 6.5.3.

10 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 6 January 2015.

11 NER, cl. 6.5.3.

Table 8.4 sets out our final decision on the standard tax asset lives for SA Power Networks.

Table 8.4 AER's final decision on SA Power Networks' standard tax asset lives (years)

Asset class	Standard tax asset life
Sub-transmission lines	55.0
Distribution Lines	55.0
Substations	45.0
Distribution Transformers	45.0
LVS	55.0
Communications	15.0
Contributions	40.2
Land	n/a
Substation land	n/a
Easements	n/a
Buildings	40.0
Vehicles - 15 years	15.0
Vehicles - 10 years	10.0
Light vehicles	5.0
IT	5.0
Plant & tools/Office furniture	10.0
Equity raising costs	5.0

Source: AER analysis.
n/a not applicable.